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

VIA ELECTRONIC FILING

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

Dear Acting Assistant Secretary Khawar,

The Center for American Progress (CAP or "we") respectfully submits this letter in support of the Department's proposed rule, *Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights* (the "proposed rule").

As a nonprofit policy institute dedicated to improving the lives of all Americans, including American workers, CAP has been a leader in promoting policies that help people climb the ladder of economic mobility and secure a stable retirement.

In 2020, under the prior administration, the Department of Labor (the "Department") enacted rules that effectively prohibited Employee Retirement Income Security Act (ERISA) plan fiduciaries from considering climate and other ESG factors in their investment selections and investment courses of action, as well as in their exercise of proxy voting.[1] As noted by the Department, the 2020 rules (the "current" rules or "2020 ESG rule") have created significant confusion, discouraged ERISA fiduciaries from considering investments that are widely viewed as prudent,[2] and continued to raise serious concerns that they will expose plan participants and beneficiaries to the negative economic impacts of climate change and other ESG factors.[3]

We believe the proposed rule addresses these concerns in an appropriate and necessary manner that resolves problems with certain new policies contained in the current rules while

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[1] Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 72846 (Nov. 13, 2020) and Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 81658 (December 16, 2020).
[2] See, e.g., "Fiduciary Duty in the 21st Century, Final Report," Principles for Responsible Investment, 2019, available at https://www.unpri.org/fiduciary-duty/fiduciary-duty-in-the-21st-century-final-report/4998.article.
[3] Although the best solution is for the Department to fix the 2020 rules, the ongoing nature and significance of concerns over the rules have also motivated legislators to seek solutions. See, e.g., "Financial Factors in Selecting Retirement Plan Investments Act," S.1762, 117th Cong., 1st sess. (May 20, 2021, available at https://www.congress.gov/bill/117th-congress/senate-bill/1762/text.

upholding longstanding Department policies around the duties of prudence and loyalty. By correcting the concerns, the proposed rule would provide managers of retirement plans the flexibility to evaluate all factors that impact plan investments, including the physical risks of climate change and the economic shifts resulting from the transition to a low-carbon economy. The risks and opportunities associated with climate change have already begun and will continue to unfold over the course of this decade and beyond, making this a particularly important consideration for the long horizons of retirement plans. Plan fiduciaries must be positioned to protect their plan participants and beneficiaries, and the proposed rule accomplishes this.

General comments:

The legally unsupportable 2020 ESG Rule was rushed through the rulemaking process despite the overwhelming opposition of stakeholders,[4] creating uncertainty and roadblocks to ESG investing, which in turn caused plan fiduciaries to shy away from such investments. The Department's decision now to initiate a procedurally-sound notice and comment rulemaking process to address those uncertainties and roadblocks is highly appropriate and certainly necessary to ensure that plan investments are the result of a prudent fiduciary process and thus protect plan participants and beneficiaries. CAP agrees with the Department that "the changes proposed will improve the current regulation and further promote retirement income security and further retirement savings." We commend the Department on addressing new policies contained in the current rule that were the subject of confusion while avoiding upending longstanding views of the agency regarding standards for selection of investments and investment courses of action or the exercise of shareholder rights, including the voting of proxies.

Comments regarding fiduciaries' duty of prudence:

CAP strongly supports the proposed rule's recognition 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." Indeed, at a time when evidence is growing about the risks to companies associated with climate change and other ESG issues,[5] leaving the 2020 ESG rule in place would further chill fiduciaries' consideration of these factors and put

[4] 95 percent of commenters expressed opposition to "Financial Factors in Selecting Plan Investments." Julie Gorte, et al., "Public Comments Overwhelmingly Oppose Proposed Rule Limiting the Use of ESG in ERISA Retirement Plans," August 20, 2020, available at https://www.ussif.org/Files/Public_Policy/DOL_Comments_Reporting_FINAL.pdf.

[5] See, e.g., S&P Global, "The Big Picture on Climate Risk," January 6, 2020, available at https://www.spglobal.com/en/research-insights/featured/the-big-picture-on-climate-risk (showing physical climate risks for companies in the S&P 500 Index); and Deloitte, "Feeling the heat?" December 12, 2019, available at https://www2.deloitte.com/us/en/insights/topics/strategy/impact-and-opportunities-of-climate-change-on-business.html (discussing the multiple impacts of climate change on companies, including increased business risks, physical risks, and transition risks such as "changes in technologies, markets and regulations that can increase business costs, undermine the viability of existing products or services, or affect asset values.")

retirement funds in jeopardy. We also note in this regard the extensive evidence of the value of taking climate and other ESG factors into account in investment practices.[6]

If left in place, the 2020 ESG rule would overturn the Department's longstanding policy that ESG factors may be relevant and warrant consideration by a prudent fiduciary when evaluating the risk and return of investment opportunities, and further that in many situations evaluation of ESG factors is required by prudent fiduciaries, especially given the long-term investment horizons of defined benefit and many defined contribution plans. This is true not just with respect to the growing physical harms caused by climate change but also the anticipated law and policy changes that businesses will face as the economy transitions to a low-carbon future. These changes will create significant shifts in the value of different investments across the markets, giving rise to potentially serious risks to plan participants and beneficiaries.

The shifts have already begun in the energy sector, for example, which highlights the importance of fixing the 2020 ESG rule. In its report "Modernizing the Social Contract With Investment Fiduciaries," CAP pointed to the fact that the energy sector of the S&P 500 has been in trouble for a decade and has underperformed the rest of the index since 2014. An ESG-minded investor who decided 10 years ago to invest in the S&P 500 but exclude the energy components, which are almost exclusively oil and gas firms, would have significantly outperformed the overall market.[7] Sophisticated investors are aware of the risks and opportunities presented by climate change and other ESG issues. They are addressing climate risk as an important principle of capital preservation and growth.[8]

In light of the above, CAP strongly supports the Department's proposed clarifications in paragraph (B)(4) that climate and ESG factors are just like any other factor relevant to the risk-return analysis. We especially support the Department's list of examples of such factors—

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[6] See, e.g., Morgan Stanley, "Sustainable Reality: Analyzing Risk and Returns of Sustainable Funds," Morgan Stanley, 2019, available at https://www.morganstanley.com/content/dam/msdotcom/ideas/sustainable-investing-offers-financial-performance-lowered-risk/Sustainable_Reality_Analyzing_Risk_and_Returns_of_Sustainable_Funds.pdf. (Finding that "there is no financial trade-off in the returns of sustainable funds compared to traditional funds, and they demonstrate lower downside risk."); Jon Hale, "Sustainable Equity Funds Outperform Traditional Peers in 2020," Morningstar, January 8, 2021, available at https://www.morningstar.com/articles/1017056/sustainable-equity-funds-outperform-traditional-peers-in-2020; Tensie Whelan, Ulrich Atz, Tracy Van Holt and Casey Clark, "ESG and Financial Performance, Rockefeller Asset Management and NYU Stern Center for Sustainable Business, 2021, available at https://www.stern.nyu.edu/sites/default/files/assets/documents/NYU-RAM_ESG-Paper_2021%20Rev_0.pdf; Claudia Goldin, "Human Capital," *Handbook of Cliometrics* (2014): 1-42, available at https://scholar.harvard.edu/files/goldin/files/human_capital_handbook_of_cliometrics_0.pdf; and Hernando Cortina, "Just Business, Better Margins" (New York: JUST Capital, 2019), available at https://justcapital.com/wp-content/uploads/2019/06/JUSTCapital_JBBM_FullReport_06102019.pdf.

[7] Tyler Gellasch and Alexandra Thornton, "Modernizing the Social Contract With Investment Fiduciaries," (Washington: Center for American Progress, 2020), available at https://www.americanprogress.org/article/modernizing-social-contract-investment-fiduciaries/.

[8] See, e.g., "2021 Global Investor Statement to Governments on the Climate Crisis," *The Investor Agenda,* 2021, available at https://theinvestoragenda.org/wp-content/uploads/2021/09/2021-Global-Investor-Statement-to-Governments-on-the-Climate-Crisis.pdf (last accessed December 2021).

which provide clarity for fiduciaries as to the meaning of this paragraph and the duty of prudence.

We recommend that these examples remain in the text of the rule and that the Department consider the following minor changes: As referenced in the language of the proposed rule, we strongly recommend that this list of examples be accompanied by a statement that the list is not exclusive, to eliminate any doubt about the scope of the paragraph and avoid future unnecessary harm to plan participants and beneficiaries from failure to consider important factors that were not listed. We further suggest that the term “social” be included, referencing “workforce practices” as an example, and that the term “human capital” be included in addition to “workforce practices.” We are also in agreement with those who have suggested that the language should be clarified to reflect that climate change is one example of an environmental issue that should be considered. All of these minor changes would avoid any negative inferences and would reflect the language used by countless corporate managers, investors and asset owners.

We would urge the Department to remove the term “material” and substitute the term “relevant” in the following language of Subparagraph (b)(4): “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…” Ever since the Department adopted the investment duties regulation, the ERISA standard has been for the fiduciary to consider all “relevant” factors.[9] There is no justification for introducing this new term in the standard, one that has not been part of this ERISA fiduciary standard until it was improperly and unnecessarily inserted in the 2020 ESG rule. Leaving this term in the language of the rule will only perpetuate the confusion and uncertainty around the 2020 ESG rule and could be used improperly to avoid compliance with ERISA duties through false analogies to the term as used in the federal securities laws.

Comments regarding fiduciaries’ duty of loyalty:
CAP finds that the cross-referencing and clarification that economically relevant climate and other ESG factors are consistent with the duty of loyalty makes eminent sense, along with the elimination of a separate definition of “pecuniary,” which caused much confusion and concern when it was introduced in the 2020 ESG rule, since many relevant financial factors that have pecuniary impacts also have non-pecuniary affects, such as climate risks.

We applaud the Department’s proposal to rescind the “tie-breaker” standard in the current rule, which states that competing investments are only tied when they are “indistinguishable” based on risk and return. The proposed rule’s remedy for this unrealistically narrow rule is to allow the fiduciary to choose between competing investments and courses of action when the alternatives “equally serve the financial interests of the plan.” While the proposed language is quite an improvement over the language in the 2020 ESG rule, language that more clearly reflects the examples in the Preamble would be preferable. ERISA fiduciaries usually employ a

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[9] See, Investment Duty Regulation, 29 CFR 2550.404a-1(b)(1)(i), 44 Fed. Reg. 37221-37225 (June 26, 1979). “Relevant” factors was restated several times recently by the Department. See, e.g., Interpretive Bulletin 94-1, 59 Fed. Reg. 32606 (June 23, 1994); Interpretive Bulletin 2008-01, 73 Fed. Reg. 61734 (October 17, 2008); and Interpretive Bulletin 2015-01, 80 Fed. Reg. 65135 (October 26, 2015).

prudent investment process that results in multiple investments meeting the plan's criteria, making any one of them "prudent." In these cases, the plan fiduciary should be able to choose any one of these investments without further justification or special documentation.

We believe the Department is making the right choice to directly rescind the current regulation's documentation requirements when a fiduciary concludes that pecuniary factors alone were insufficient to be the deciding factor. The documentation requirement in the current rule effectively targets climate and ESG factors, unnecessarily chilling fiduciaries' choices of these investments, and is potentially harmful to plan participants and beneficiaries.

Finally, CAP concurs with the decision in the proposed rule not to carry forward the prohibition against certain investment alternatives being used as QDIA, which the Department correctly observes "only serves to harm participants by depriving them of otherwise financially prudent options as QDIAs."

Comments on Proxy Voting and Exercise of Shareholder Rights:
CAP supports the Department's proposed rule with regard to the elimination of specified provisions of the current rule, including the current rule's statement that "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;" the two so-called "safe harbors," which are unnecessary and could discourage fiduciaries from properly representing participants' interests; and the recordkeeping provisions of the current rule, which are unnecessary, costly to fiduciaries, and create the impression that proxy voting and exercising of shareholder rights are not favored. We fundamentally agree with the Department's assessment that "fiduciaries should take their rights as shareholders seriously and conscientiously exercise those rights to protect the interest of plan participants."

In conclusion, we believe the Department's action, through the proposed rule, to address the arbitrary and harmful provisions of the referenced 2020 rules on fiduciary duties in selecting plan investments and exercising shareholder rights is both appropriate and necessary. It upholds and further clarifies longstanding policies of the Department and will go a long way toward protecting the interests of workers who participate in employee benefit plans, retirees, and plan beneficiaries in the decades ahead.

Please do not hesitate to contact me or my colleagues if there are any questions regarding these comments.

Sincerely,

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