

We the undersigned appreciate the opportunity to respond to the Request for Information (“RFI”) published by the Employee Benefits Security Administration (“EBSA”) in the Federal Register on February 14, 2022 [87 FR 8289].

Douglas Kant is an ERISA lawyer who practiced as in-house counsel with a major financial services firm. Although now retired from full-time employment, he stays involved with the benefits world and has closely followed the debate over environmental, social and governance (“ESG”) issues in the development of EBSA guidance. He previously submitted comments on the EBSA proposal that would revise the Investment Duties rule issued near the end of the previous administration. Gita Rao is a Senior Lecturer in Finance and Associate Faculty Director of the Master of Finance program at the MIT Sloan School of Management. Her focus includes fund proxy voting on ESG-related issues. She has also worked for many years as an investment analyst, research director and portfolio manager for several investment management firms.

The following comments only respond to some of the question posed in the RFI and, for convenient reference, the comments below are numbered to correspond to the number of the RFI question addressed by the comment.

(1) We appreciate the Department’s current effort to undo the impact of the 2020 Investment Duties regulation, which has had the effect of undermining the consideration of ESG issues in investment decision-making. Although not completely clear in the 2020 final rule, the 2020 rule preamble appeared to portray ESG issues as a “suspect class” in investment decision-making. The new proposed rule would directly reverse that bias in the regulation. At this point EBSA is in an information gathering mode (thus this RFI) and it seems that further attempts to issue guidance addressing climate-related financial risk may be premature, however, please see the response to question 5 below.

(2) A complete list of significant climate-related financial risks may not be compiled as of this moment, but we suggest the following divided into physical and transitional risk categories as referenced by the RFI.

Presidential Executive Order 14030 (dated May 20, 2021), which directed many government organizations or administrative bodies including the Department of Labor to assess climate-change financial risk, refers to physical risk to assets, publicly traded securities, private investments, and companies:

- (1) worsening air quality (greenhouse gas impact) creating health risks
- (2) rising sea levels (melting ice caps) that threaten coastal locations
- (3) warming oceans and seas that threaten fishing industries
- (4) rising air temperature and more volatile weather patterns (such as tornadoes), creating greater risks of major forest fires, crop damage, and structural damage and increasing the adverse effect of poor air quality
- (5) droughts, creating greater risks of major forest fires and crop damage
- (6) insurer losses from any of the above

Presidential Executive Order 14030 also refers to the global shift away from carbon-intensive energy sources and industrial processes that presents transitional risk to many companies, communities, and workers:

(1) physical locations at risk, requiring relocation of premises and staffs and the loss of some properties currently in use

(2) changes in technology, requiring major retooling of industries, residences

(3) governmental penalties for the use of current technology or resources

(3) changes in government subsidies and tax credits for specific types of technology

(4) We do not think that the annual return for benefit plans (Form 5500 series) is an appropriate vehicle for collecting climate-change information at this point. First, the current format is data-based (numbers) rather than narrative in format and we don't think it would be helpful to attempt to add a new section or schedule which is narrative in format. Second, the annual return does not ask for any information on any other criteria used by managers or advisers in selecting investments.

(5) The use of a survey or information request would certainly provide an alternative source of information for EBSA in determining whether additional guidance would be warranted. It may be useful, for example, to ask for information regarding the types of information requested by hiring fiduciaries in discharging their due diligence with respect to ESG considerations. It may be best to shorten any requests for information sent to smaller plans.

(6) We would recommend against requiring plan administrators to publicly report on steps taken to manage climate-related financial risk at this point. Among other concerns, the current lack of a clear legal disclosure framework would result in attempts to provide the least definitive response.

(7) There is an ever-increasing supply of sources of climate-change data. Many accounting firms, consulting firms and management firms are offering ESG assessment tools. We think that more diverse organizations would provide a broader perspective and encourage a more consistent response.

We want to express particular confidence in the periodic reports of the Task Force on Climate Change Financial Disclosures ("TCFD"). The most recent annual report was dated October 14, 2021. The TCFD was established by the Financial Stability Board ("FSB"), an international body that monitors and makes recommendations about the global financial system. The FSB promotes international financial stability; it does so by coordinating national financial authorities and international standard-setting bodies as they work toward developing strong regulatory, supervisory and other financial sector policies. The FSB, working through its members, seeks to strengthen financial systems and increase the stability of international financial markets. The policies developed in the pursuit of this agenda are implemented by jurisdictions and national authorities.

We would also recommend the work of the Sustainable Accounting Standards Board, which is a non-profit organization founded in 2011 to develop sustainability accounting standards.

Investors, lenders, insurance underwriters and other providers of financial capital need to assess the impact of ESG factors on the financial performance of companies, driving the need for standardized reporting of ESG data.

Another resource is the International Sustainability Standards Board (“ISSB”), established to develop a comprehensive global baseline of sustainability disclosures for the capital markets. ISSB launched a consultation on its first two proposed standards on 31 March 2022. One sets out general sustainability-related disclosure requirements, and the other specifies climate-related disclosure requirement. Upon finalization these proposals would form a comprehensive global baseline of sustainability disclosures designed to meet the information needs of investors in assessing enterprise value. The proposals have been developed in response to requests from G20 leaders, the International Organization of Securities Commissions (IOSCO) and others for enhanced information from companies on sustainability-related risks and opportunities.

(15) Question 15 of the RFI notes that the Thrift Savings Plan for Federal Government employees (TSP) uses passive index funds. The RFI question is whether there any evidence that the indexes do not properly assess climate-related financial risks.

As stated in the RFI, the investment menu for TSP does not include any actively managed funds:

There is a short-term U.S. Treasury securities fund.

There is a bond fund based on the Bloomberg Barclays US Aggregate Bond Index.

There are three equity funds:

- based on the Dow Jones US Completion Total Stock Market Index

- based on the Standard and Poor's 500 Index

- based on the MSCI EAFE (Europe, Australasia, Far East) Index

There is also a series of life cycle funds in the lineup, but the components for each life cycle fund are comprised entirely of differing amounts of the funds listed above.

Clearly these indexes don't directly take ESG issues into account; investments in each fund are determined by the issuer's size compared with other issuers represented in the index. One could try to argue that companies in the index are successful in part because they take ESG issues into account, but that does not seem to be a particularly compelling argument at this point in time.

We understand from a final rule notice published in the Federal Register on May 10, 2022 [87 FR 27917], that TSP will begin to offer a mutual fund window to participants next month, which will allow TSP participants to invest in thousands of mutual funds advised by many different fund advisers. Although we don't know at this point which mutual funds will be offered through the window, the sheer number of funds seems to dictate that some of the funds will address ESG considerations. The restrictions included in the final rule limit the percentage of a participant's account that may be invested through the window. Although the stated desire to ensure that offering the window does not increase the cost of participation for those who don't use the window is laudable, the expense for those who consider the window (a \$55 annual fee, a \$95 annual maintenance fee, and a \$28.75 per trade fee, as well as any fees or expenses imposed by the specific fund in which the participant invests) may deter some or many who would otherwise use it.

Another challenge for TSP participants who use the mutual fund window may be the sheer number of choices confronted by a participant who wants to include ESG considerations in their choices. We don't know if the funds will only be grouped by adviser or asset class, for if other criteria may be used, but this is an issue that should be considered by the Federal Retirement Thrift Investment Board if it has not already done so.

(19) Although most IRA and many 403(b) accounts are not subject to the fiduciary and prohibited transaction provisions of ERISA, advisers and other service providers for these accounts are generally subject to obligations under securities, banking and insurance laws protective of their customers. The regulators with jurisdiction in such matters would be required to assess those obligations.

As an example, we reference the SEC proposed rule published in the Federal Register on April 11, 2022 [87 FR 21334], which is intended to enhance and standardize climate-related disclosures for investors in public companies. The proposed disclosures would include the disclosure of a registrant's greenhouse gas emissions as well as the material impact of climate-change on the various aspects of a company's business operations.

(20) We do not believe that EBSA is adequately staffed to improve data and analytics on climate-change financial risk. These issues are complex and require specialized resources as well as personnel and training, and we respectfully submit that other organizations are better resourced to handle such matters.

(21) It seems apparent that coordination between EBSA and the SEC would be crucial to provide a clear and consistent message to plan participants in participant-directed individual account plans on climate-change financial risk. The wide variations in plan investment offerings will greatly complicate any official communications on this topic.

(22) Although Treasury/IRS and the SEC have primary jurisdiction over non-ERISA IRAs and 403(b)s and certain States have primary jurisdiction over their automatic IRA arrangements for private employers, it again makes sense to promote coordination among those regulators and EBSA to try to provide a clear and consistent message to the individual account owners or annuity contractholders.

Thank you for your consideration. We would be pleased to respond to any questions or comments from the EBSA staff.

Douglas Kant, Esq.
dougokant@gmail.com
(617) 548-1629

Gita R. Rao, PhD
Senior Lecturer in Finance, Associate Faculty Director (Master of Finance program)
MIT Sloan School of Management.
grao@mit.edu
(617) 324-7247