July 30, 2020

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

Re: Department of Labor RIN 1210-AB95, "Financial Factors in Selecting Plan Investments"

Dear Assistant Secretary Wilson,

The Interfaith Center on Corporate Responsibility (ICCR) is a broad coalition of institutional investors collectively representing over $500 billion in invested capital. ICCR members, a cross section of faith-based investors, asset managers, pension funds, foundations, and other long-term institutional investors, have nearly 50 years of experience engaging companies on environmental, social, and governance ("ESG") issues that are critical to long-term value creation. ICCR members fundamentally believe that companies that meaningfully address environmental and social risks, and that have strong and accountable governance practices, are companies that are best positioned for long-term success.

ICCR and the 138 member signatories to this comment letter write to express our strong opposition to the Department of Labor's (the "Department's") proposed rule, "Financial Factors in Selecting Plan Investments" (the "Proposed Rule"), set forth in the Notice of Proposed Rulemaking ("NPRM").[1] The Proposed Rule would impose significant analytical and documentation burdens on fiduciaries of benefit plans governed by the Employee Retirement Income Security Act ("ERISA") wishing to select (or allow individual account holders to select) investments that use ESG factors in investment analysis or that provide ESG benefits.

We are concerned that the Proposed Rule will deter consideration of ESG factors by ERISA fiduciaries, and perhaps others whose regulatory frameworks follow ERISA, despite ample evidence that integrating such factors can improve performance. While not all of ICCR's members are governed by ERISA, we are further concerned that the NPRM broadly calls into question, with no factual basis, not only "ESG-themed" investment products but also ESG ratings and the use of ESG factors in traditional investment analysis.

The NPRM does not establish either that the Proposed Rule is necessary or that it would provide appreciable benefits, and it fails to analyze costs to plans and their participants and

1 Financial Factors in Selecting Plan Investments (RIN 1210-AB95), 85 Fed. Reg. 39113 (June 30, 2020).

beneficiaries. These major shortcomings preclude an adequate cost-benefit analysis. Accordingly, we strongly urge the Department to withdraw the Proposed Rule.

Background--ESG and Investing

Consideration of ESG factors in investing has achieved widespread acceptance both in the U.S. and globally in recent years, since ICCR members began engaging with companies about environmental, social, and governance issues in the early 1970s. Although much of the NPRM focuses on investments promising moral or ethical ESG benefits, major growth has occurred in integration of ESG considerations in order to improve portfolio company performance.[2] According to a survey by RBC Global Asset Management, 70% of institutional investors in Canada, the U.S. and the U.K. "apply ESG principles to investment decisions," with 53% of respondents citing mitigation of risk and higher returns as reasons for doing so.[3]

The CFA Institute, a global association of investment professionals, has stated that it believes that the requirement that investment professionals weigh all material information "includes the consideration of material ESG information/considerations (ESG factoring) as an important component of a complete and thorough financial analysis for any actively managed fundamental investment portfolio."[4] "ESG Investing and Analysis" is one of three areas of "research and thought leadership" featured on the organization's home page.[5] The Principles for Responsible Investment boasts over 3,000 signatories with more than $100 trillion in assets under management; signatories commit to "incorporat[ing] ESG issues into investment analysis and decision making processes."[6]

In his 2020 letter to CEOs, Larry Fink, the Chairman and CEO of BlackRock, the world's largest asset manager, announced that BlackRock would "place sustainability at the center of [its] investment approach" and asserted that "[c]limate change has become a defining factor in companies' long-term prospects." Similarly, State Street Global Advisors President and CEO Cyrus Taraporevala recently noted: "Having already engaged with companies on a number of governance matters for many years, we see that shareholder value is increasingly being driven by issues such as climate change, labor practices, and consumer product safety. We believe that addressing material ESG issues is good business practice and essential to a company's long-term financial performance..."[7] The Business Roundtable, an association of large U.S. company CEOs, has recognized the importance of ESG considerations; last year, it issued a

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[2] See https://corpgov.law.harvard.edu/2020/03/02/top-10-esg-trends-for-the-new-decade/; https://personal.vanguard.com/pdf/ISGESG.pdf; https://www.bsr.org/reports/BSR_Trends_in_ESG_Integration.pdf; https://www.ussif.org/files/Publications/SIF_Trends_14.F.ES.pdf

[3] Hazel Bradford, ""70% of Institutional Investors Apply ESG to Investment Decisions—Survey," *Pensions & Investments*, Oct. 16, 2019 (https://www.pionline.com/esg/70-institutional-investors-apply-esg-investment-decisions-survey)

[4] https://www.cfainstitute.org/-/media/documents/article/position-paper/cfa-institute-position-statement-esg.ashx

[5] See https://www.cfainstitute.org/

[6] https://www.unpri.org/pri/about-the-pri

[7] https://www.ssga.com/us/en/individual/etfs/insights/informing-better-decisions-with-esg (emphasis in original)

"Statement on the Purpose of the Corporation" articulating a "fundamental commitment" to all stakeholders, including respecting "people in our communities" and protecting the environment.[8]

Empirical evidence indicates that better ESG performance is associated with lower idiosyncratic risk, lower probability of financial distress/bankruptcy, more positive analyst recommendations, lower cost of capital, and superior returns.[9] A study of shareholder engagements on environmental and social issues found that successful engagements led to higher sales growth and that successfully engaged firms with low ESG scores prior to engagement had statistically significant excess cumulative abnormal returns compared with similar non-engaged firms in the year following closure of the engagement.[10] A 2016 study found, among other things, that firms with high corporate social responsibility ("CSR") ratings are valued more highly than firms with low ratings, and firms with higher CEO pay-performance sensitivity and firms in jurisdictions with stronger legal protections for shareholders engage in more CSR activities, which supports a conclusion that CSR is value-enhancing.[11]

Insufficient Economic Justification and Flawed Cost/Benefit Analysis

The NPRM's justification for the Proposed Rule is speculative and poorly supported, suggesting that the Department is motivated more by political hostility to ESG issues than by a well-founded concern for plan participants and beneficiaries. The NPRM expresses worry that "the growing emphasis on ESG investing, and other non-pecuniary factors, may be prompting ERISA plan fiduciaries to make investment decisions for purposes distinct from their responsibility to provide benefits to participants and beneficiaries and defraying reasonable administrative expenses."[12] But the statistics cited in the NPRM do not track the proposed solutions to this supposed problem, as they conflate "ESG investing," "consider[ing] ESG factors in investment decisions," "ESG-themed" investment options, and "socially responsible" equity funds.[13]

No effort is made to assess the extent to which any of these products or approaches explicitly aim to provide non-pecuniary benefits—choices to which the Proposed Rule's "tie-breaker" provision applies--as opposed to considering ESG factors as part of traditional investment

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[8] Business Roundtable, "Statement on the Purpose of a Corporation" (2019) (https://opportunity.businessroundtable.org/wp-content/uploads/2019/12/BRT-Statement-on-the-Purpose-of-a-Corporation-with-Signatures.pdf)

[9] See Allen Ferrell et al., "Socially Responsible Firms," at 2-3 (2016) ("Ferrell Study")(available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2464561); https://hbr.org/2019/05/the-investor-revolution; https://institutional.dws.com/content/_media/K15090_Academic_Insights_UK_EMEA_RZ_Online_151201_Final_(2).pdf; https://newsroom.bankofamerica.com/system/files/2019_Environmental_Social_Governance.pdf

[10] https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2977219; https://www.bsr.org/reports/BSR_Trends_in_ESG_Integration.pdf

[11] Ferrell Study, supra note __, at 21-22, 25, 30.

[12] NPRM, at 39120.

[13] NPRM, at 39120-39121.

analysis.[14] The NPRM cites a law review article that defines the former as "collateral benefits" ESG investing and the latter as "risk-return" ESG investing, but often refers to the two concepts interchangeably.[15] Without some idea of the prevalence of each among ERISA-governed funds, it is not possible to analyze the benefits and costs of the Proposed Rule's differing approaches to collateral benefits and risk-return investing.

Nor does the NPRM evaluate the financial performance of various types of ESG investing compared to non-ESG counterparts. There is evidence that ESG funds, indices and portfolios outperform market and other benchmark indices over at least some periods.[16] Reporting on the first quarter of 2020, BlackRock noted that it "observed better risk-adjusted performance across sustainable products globally, with 94% of a globally-representative selection of widely-analyzed sustainable indices outperforming their parent benchmarks." That performance, according to BlackRock, "aligns with the resilience we have seen in sustainable strategies during prior downturns" and is attributable to a "range of material sustainability characteristics, including job satisfaction of employees, the strength of customer relations, or the effectiveness of the company's board."[17] The absence of such a discussion in the NPRM may reflect the fact that burdening fiduciaries' ability to select investments that outperform is more fairly characterized as a regulatory cost than a benefit.

The NPRM's analytical fuzziness and lack of performance data limit the Department's ability to quantify, even in a rough way, the benefits of the Proposed Rule. The NPRM's assertion that "[t]o the extent that ESG investing sacrifices return to achieve non-pecuniary goals, it reduces participants' and beneficiaries' retirement investment returns,"[18] is purely speculative. As well, the NPRM makes contradictory claims about the extent to which plan fiduciaries are violating existing sub-regulatory guidance on the issues addressed by the Proposed Rule. On the one hand, the NPRM asserts that the Proposed Rule would provide the benefit of "eliminat[ing] confusion that plan fiduciaries may currently face."[19] In the next breath, however, the NPRM states that the Department believes that the number of plan fiduciaries that are not following or misinterpreting the guidance is "small."[20] If nearly all fiduciaries are following the guidance, why is the Proposed Rule necessary? Given the great

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[14] The NPRM cites a law review article that defines the former as "collateral benefits" ESG investing and the latter as "risk-return" ESG investing. NPRM, at 39120 (citing Max Schanzenbach & Robert Sitkoff, "Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing by a Trustee," 72 Stan. L. Rev. 381, 392-97 (2020)).

[15] NPRM, at 39120 (citing Max Schanzenbach & Robert Sitkoff, "Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing by a Trustee," 72 Stan. L. Rev. 381, 392-97 (2020)).

[16] E.g., https://www.forbes.com/sites/brendancoffey/2019/11/12/esg-stocks-are-having-a-fantastic-year/#298759412fbb; https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/major-esg-investment-funds-outperforming-s-p-500-during-covid-19-57965103; https://www.morningstar.com/articles/976361/sustainable-funds-weather-the-first-quarter-better-thanconventional-Funds; https://www.top1000funds.com/wp-content/uploads/2013/01/Optimizing-ESG-Factors-in-Portfolio-Construction.pdf

[17] https://www.blackrock.com/corporate/literature/investor-education/sustainable-investing-resilience.pdf, at 3.

[18] NPRM, at 39121.

[19] NPRM, at 39119.

[20] NPRM, at 39120.

uncertainty about the benefits of the Proposed Rule, continuing with the sub-regulatory guidance should have been one of the alternatives to the Proposed Rule considered in the NPRM.

In addition to this deficient showing on purported benefits, the NPRM does not adequately support its analysis of potential costs associated with the Proposed Rule. The NPRM concludes that the Proposed Rule would not impose "a significant increase in hourly burden or cost" because the true "ties" between "economically indistinguishable" investments that would permit a fiduciary to choose the one that provides a collateral ESG benefit "occur very rarely in practice, if at all."[21] The only basis provided for that conclusion is a single law review article referring to such equivalent investments, without support, as "unicorns."[22] Thus, the NPRM's conclusion regarding costs of complying with the tie-breaker provision of the Proposed Rule completely lacks support.

Potential foregone benefits that would flow from reducing ESG investing are not limited to those related to a specific investment decision. Investing in which ESG considerations play a role, especially the type of engagement with portfolio companies that ICCR members have led for decades, can bring about changes in corporate behavior that protect the value of other securities across the portfolio, as well as investments in other asset classes. Larry Fink points out in his recent CEO letter that climate impacts span asset classes[23]; thus, curbing greenhouse gas emissions by a company whose equity security a plan holds may protect value not only of the plan's investment in that company, by allowing it to avoid disruptions from impending regulations, but also for the plan's real estate investments, which face physical risk from climate change.

Taking steps to prevent catastrophic warming would also reduce risks to the global financial system and the broader economy.[24] These changes in behavior could well be reduced by the Proposed Rule, and the Department has an obligation to identify and analyze the potential negative impacts to companies, sectors, the financial system and the economy. Indeed, where ESG factors are material, we believe that the Department should clarify for ERISA fiduciaries that the duty of care under section 404(a)(1)(B) of ERISA requires their consideration, rather than imposing additional analytic and documentation burdens as the Proposed Rule now does.

The Proposed Rule's Tie-Breaker Standard is at Odds with its Ostensible Purpose

The long-standing purpose of the tie-breaker test, which has been in effect for years in the Department's sub-regulatory guidance, has been to ensure that a fiduciary does not accept lower expected returns or assume greater risks in order to obtain collateral benefits. Guidance issued in 2018 reaffirmed that standard.[25]

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21 NPRM, at 39123, 39125.
22 Rulemaking, article cite
23 https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter
24 See https://www.ceres.org/sites/default/files/reports/2020-06/Financial%20Regulators%20FULL%20FINAL.pdf;
25 See Field Assistance Bulletin (FAB) 2018-01.

The Proposed Rule goes far beyond the traditional tie-breaker test, which focused on risks and expected returns. The new test would require any investment option a fiduciary wants to choose based (in whole or in part) on non-pecuniary (or collateral benefit) reasons to be identical in every way, including fee structure, performance history, investment strategy, asset composition, and investment strategy, to an alternative investment except for the non-pecuniary benefit. Such an identical alternative investment might well be unavailable in the market, which would preclude a fiduciary from making the required comparison and thus from choosing the investment with the non-pecuniary benefit. The impossibility of satisfying this standard suggests that the test is designed to deter fiduciaries from considering investments with collateral benefits.

The proposed standard for defined contribution plan investment options is even more onerous. It requires that a fiduciary use "only objective risk-return criteria" to choose investment alternatives, which seems to place even the tie-breaker test off-limits. The rule for defined contribution plans also defines ESG investing more broadly: rather than an investment choice that provides collateral ESG benefits, the rule applies anytime a fiduciary wants to add "one or more prudently selected, well managed, and properly diversified investment alternatives that include one or more environmental, social, corporate governance, or similarly oriented assessments or judgments in their investment mandates, or that include these parameters in the fund name."[26]

It is unclear what an ESG "assessment or judgment" is, or what it means for such a determination to be included in the investment mandate. Would an actively managed fund whose prospectus states that it does not aim to provide non-pecuniary ESG benefits and does not include ESG in its name but does incorporate ESG data into its traditional investment analysis fall within this provision? The NPRM does not discuss the reason the Proposed Rule treats decisions made by defined benefit and defined contributions fiduciaries differently, but absent a compelling justification, the same test—the existing tie-breaker test—should apply to both.

Finally, the standard for deeming an ESG factor to be pecuniary includes too many subjective terms and burdensome requirements, which we believe will have a chilling effect. ESG "or other similarly oriented considerations," whatever the latter are, "are pecuniary factors only if they present economic risks or opportunities that qualified investment professionals would treat as material economic considerations under generally accepted investment theories."[27] Unpacking that provision reveals several thorny questions, involving subjective judgments, with which a fiduciary would need to grapple. Reasonable, informed people can disagree about these assessments, like whether a consideration is material to a particular industry or company or the view a qualified investment professional would take on that question. How do generally accepted investment theories, which tend to be basic finance theories like diversification and the capital asset pricing model, apply to something as granular as ESG

[26] NPRM, at 39127.
[27] NPRM, at 39127.

considerations? This standard contains numerous potential pitfalls designed to make it difficult and risky for a fiduciary to select an investment that has taken the uncontroversial step of incorporating ESG factors into traditional investment analysis. All of this is being proposed without any evidence whatsoever that fiduciaries' choices of such investments have resulted in lower returns or higher risk.

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For all of the above reasons, we strongly urge the Department of Labor to withdraw the Proposed Rule.

We appreciate this opportunity to provide our views on this important matter. Please feel free to contact Josh Zinner (jzinner@iccr.org) with any questions.

Sincerely,

Josh Zinner
CEO
Interfaith Center on Corporate Responsibility

ICCR Member Signatories:

444 S Foundation
Adrian Dominican Sisters, Portfolio Advisory Board
AJF Financial Services, Inc.
As You Sow
Avera Health
Benedictine Coalition for Responsible Investment
Bon Secours Mercy Health
Boston Common Asset Management
Boston Trust Walden
Brethren Foundation Funds, Inc.
BVM Shareholder Education/Advocacy Group (SEA)
Center for Social Concerns, University of Notre Dame
Christian Brothers Investment Services (CBIS)
Christian Church Foundation
Church Investment Group
Church of the Brethren Benefit Trust
Clean Yield Asset Management
ClearBridge Investments
Committee on Mission Responsibility Through Investment of the Presbyterian Church U.S.A.
CommonSpirit Health
Congregation of Sisters of St. Agnes
Congregation of St. Basil
Congregation of St. Joseph
Corporate Responsibility Office - The Province of Saint Joseph of the Capuchin Order

Dana Investment Advisors
Daughters of Charity, Province of St. Louise
Domini Impact Investments LLC
Dominican Sisters ~ Grand Rapids
Dominican Sisters of Mission San Jose
Dominican Sisters of Sparkill
Dominican Sisters of Springfield, IL
Dominican Sisters of San Rafael
Episcopal Diocese of Western Massachusetts
Ethos Foundation
Etica Sgr - Responsible Investments
Everence and the Praxis Mutual Funds
Felician Sisters of North America
Figure 8 Investment Strategies
FOR Investment Partners
Franciscan Sisters of Allegany NY
Friends Fiduciary Corporation
FSPA
Heartland Initiative
Investor Advocates for Social Justice
Investor Voice
Jessie Smith Noyes Foundation
Jesuit Committee on Investment Responsibility
Jesuits of the US Central and Southern Province
Maryknoll Fathers and Brothers
Maryknoll Sisters
Mercy Investment Services, Inc.
MicroVest Capital Management
Miller/Howard Investments, Inc.
Nathan Cummings Foundation
Newground Social Investment
Nia Impact Capital
NorthStar Asset Management, Inc.
Northwest Coalition for Responsible Investment
OIP Trust/Missionary Oblates
Priests of the Sacred Heart, US Province
Province of St. Mary of the Capuchin Order
Proxy Impact
Racine Dominicans - Socially Responsible Investment Committee
Reform Pension Board
Region VI Coalition for Responsible Investment
Religious of the Sacred Heart of Mary, WAP
Riverwater Partners
SC Group
SCC Corporate Responsibility Committee
School Sisters of Notre Dame
School Sisters of Notre Dame Cooperative Investment Fund
School Sisters of St. Francis
Seventh Generation Interfaith Inc.
SHARE
Sisters of Bon Secours USA
Sisters of Charity of Cincinnati Ohio
Sisters of Charity of New York
Sisters of Charity of Saint Elizabeth
Sisters of Charity, BVM
Sisters of Charity, Halifax
Sisters of Mary Reparatrix
Sisters of Saint Joseph of Chestnut Hill, Philadelphia, PA
Sisters of St. Dominic of Blauvelt, New York
Sisters of St. Dominic of Caldwell
Sisters of St. Francis of Philadelphia
Sisters of St. Francis-Dubuque
Sisters of St. Joseph of Baden, PA
Sisters of St. Joseph of Orange
Sisters of St. Joseph of Springfield
Sisters of St. Joseph, St. Louis, MO
Sisters of the Holy Names of Jesus and Mary

Sisters of the Humility of Mary
Sisters of the Presentation of the BVM of Aberdeeen SD
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T'ruah: The Rabbinic Call for Human Rights
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The Pension Boards-United Church of Christ, Inc.
Trillium Asset Management
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Vert Asset Management