

July 30, 2020

The Honorable Jeanne Klinefelter Wilson
Acting Assistant Secretary
Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Avenue NW
Washington, DC 20210

RE: RIN 1210-AB95 - Factors in Selecting Plan Investments Proposed Regulation

Dear Assistant Secretary Wilson:

The ERISA Industry Committee (ERIC) appreciates the opportunity to comment on the proposed rule, “Factors in Selecting Plan Investments” issued by the United States Department of Labor (Department) published in the Federal Register on June 30, 2020 (Proposed Rule). ERIC has a strong interest in the Proposed Rule because our member companies sponsor and maintain retirement plans for millions of their workers and retirees. As plan sponsors, our member companies are committed to all of their fiduciary obligations, including the investment decisions for their retirement plans. Consequently, ERIC appreciates that the Proposed Rule codifies the long-established principles of fiduciary standards for selecting retirement plan investments.

ERIC member companies supervise billions of dollars in retirement assets with the goal of providing the best financial investments and outcomes for their participants, in accordance with their fiduciary obligations. The litany of sub-regulatory guidance on fiduciary requirement for plan investments has allowed for differing interpretations of these requirements, leading to confusion and inconsistency. Moreover, the constant re-issuance of sub-regulatory guidance creates uncertainty because plan fiduciaries cannot be sure how long the sub-regulatory guidance will be in effect or what new guidance will say. In addition, the sub-regulatory guidance has followed trends of investment theories such as “social investing,” “economically targeted investing” and now “economic, social, and governance (ESG) investing.” While these theories and trends constantly change, plan fiduciaries’ obligations remain the same. Therefore, ERIC believes that codifying fiduciary obligations for investment decisions is critical to provide certainty and consistency for plan fiduciaries despite changes in investment terms, theories and trends.

The Department offers the Proposed Rule to reiterate “that plan fiduciaries when making decisions on investments and investment courses of action must be focused solely on the plan’s financial risks and returns, and the interests of plan participants and beneficiaries in their plan benefits must be paramount.” Furthermore, the Proposed Rule clarifies that “[t]he fundamental principle is that an ERISA fiduciary’s evaluation of plan investments must be focused solely on

economic considerations that have a material effect on the risk and return of an investment based on appropriate investment horizons, consistent with the plan's funding policy and investment policy objectives.” We support this clarification as sub-regulatory guidance has created the possibility for differing and changing interpretations. Due to this uncertainty, we believe that all audits of ESG funds and factors should be halted until the Department’s fiduciary principles related to ESG factors are codified in a final rule.

ERIC is the only national association that advocates exclusively for large employers on health, retirement, and compensation public policies at the federal, state, and local levels. With member companies that are leaders in every sector of the economy, ERIC is the voice of large employer plan sponsors on public policies impacting their ability to sponsor benefit plans for active and retired workers, as well as families. ERIC supports the ability of its large employer member companies to tailor retirement, health, and compensation benefits to meet the unique needs of their workforces and has a strong interest in policies that impact the ability of employers to provide effective and cost-efficient retirement and health care programs to millions of workers, retirees, and their families. As such, ERIC has a vested interest in the Proposed Rule and is well-positioned to provide helpful information.

ERIC supports the codification of the fiduciary principle requiring plan fiduciaries to focus on the financial best interest of participants. While the codification of this principle provides certainty, we are concerned that the Proposed Rule could be interpreted to increase unnecessary administrative burdens and heighten the risk of frivolous litigation for plan fiduciaries, and thus offer specific suggestions to address these concerns. We are eager to work with the Department and look forward to a final rule that provides certainty and consistency for plan fiduciaries.

Comments

ERIC Supports Codification of the Long-Established Principles of Fiduciary Standards for Selecting Investments. As mentioned in the preamble to the Proposed Rule, there has been a long history of sub-regulatory guidance attempting to explain the fiduciary standards for investment selection.¹ Beginning with Interpretive Bulletin 94-1, the Department has tried to clarify how fiduciaries should deal with non-pecuniary factors (at that time referred to as “economically targeted investments”). Since then, the Department has issued two other Interpretive Bulletins and a Field Assistance Bulletin to address non-pecuniary factors.² While there are variances among the guidance, the Department has consistently emphasized that plan fiduciaries are to focus on the plan’s financial returns and risk to participants and beneficiaries. As such, this has been the practice of plan fiduciaries.³ Nonetheless, the continued issuance of sub-regulatory guidance has raised questions and created unnecessary confusion. Consequently,

¹ 85 FR 39113, p.

² In 2008, the Department replaced IB 94-1 with Interpretive Bulletin 2008-01 (IB 2008-01). In 2015, the Department replaced IB 2008-01 with Interpretive Bulletin 2015-01 (IB 2015-01). In 2018, the Department clarified IB 2015-01 in Field Assistance Bulletin 2018-01 (FAB 2018-01).

³ As there are no absolutes, we realize that not every plan fiduciary follows this principle or practice, but our experience finds that most plan fiduciaries do.

codifying this guidance, especially with the opportunity for notice and comment, will go a long way in providing certainty for plan fiduciaries.

The Requirement to Compare “Available Alternative Investments” is Unclear. Since investments can be evaluated only through relative assessment and not in a vacuum, ERISA’s doctrine of prudence already requires that reasonable consideration be given to alternative investments or investment courses of action. However, an explicit comparison requirement implies a specific course of action, which is unclear. For example, how many “alternatives” need to be considered? Or are there specific types of alternatives to be considered? This requirement could be construed to include a comprehensive and continuous evaluation of all investment alternatives, which is neither practical nor feasible. Therefore, we recommend that the Department delete the requirement to compare available alternatives under paragraph (b)(2)(ii)(D).

The Enhanced Documentation Requirement is Unnecessary. Paragraph (c)(3)(ii) of the Proposed Rule requires that plan fiduciaries maintain additional documentation if there are ESG factors in a designated investment alternative in an individual account plan. This requirement is unnecessary because Paragraph (3)(i) sets out an appropriate standard for the selection of investment options in an individual account plan. A fiduciary must be able to prove adherence to this standard if challenged. While documentation may help prove adherence, it should not in itself be a factor of liability. In addition, it does not make sense to apply a different set of rules to one category of investments when the decision-making process for all investments should be the same. The result will be a misallocation of resources with fiduciaries unnecessarily fulfilling document requirements. In addition, it increases liability risks by creating litigation claims for simple failures to maintain adequate documentation.

Furthermore, the documentation requirement is too broad. The Proposed Rule is meant to apply only to funds with ESG factors. However, the language states that documentation is required for every investment alternative “that include[s] 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.”⁴ Thus, the requirement will apply to investments chosen for purely pecuniary factors simply because there is a mention of an ESG factor. Moreover, to ensure that this requirement is met, plan fiduciaries will essentially have to apply the documentation requirement to every investment decision to avoid an inadvertent failure. For all of these reasons, we recommend that the Department remove the documentation requirement under paragraph (c)(3)(ii) from the final rule.

The Proposed Rule Could Increase Litigation Risks for Plan Fiduciaries. While we support the codification of the principles that plan fiduciaries have been following, some of the new parts of the rule increase the potential for litigation. As mentioned above, both the requirement to compare available investment alternatives and the documentation requirement impose additional requirements that are not only unnecessary but also could increase litigation risks.

As discussed, an explicit requirement to compare “available alternative investments” could be interpreted to include a comprehensive and continuous evaluation of all investment alternatives.

⁴ 85 Fed. Reg. at 39127; Paragraph (c)(3).

Because such a comparison is impossible, it sets up the possibility that litigation could be brought for any alternative that is not considered by the fiduciary. Similarly, the documentation of ESG considerations creates a possible litigation roadmap. As explained above, the documentation requirement implements contemporaneous documentation as a factor of liability. In essence, a fiduciary could be found liable for a breach not because of the investment decision, but because of a documentation failure.

These concerns are not without reason. Over the last decade, there has been a significant increase in ERISA class action lawsuits, many frivolous with the end game of settlements that inure to the benefit of plaintiffs' legal counsel and not plan beneficiaries. The purpose of the Proposed Rule is to bring certainty to the decision-making process for fiduciaries, and this important goal should not be marred by increasing the opportunity for frivolous lawsuits.⁵

The Final Rule Should Consistently Use the Terminology “Non-Pecuniary Factors.” The Proposed Rule specifically uses the term “ESG” to describe non-pecuniary factors that are prohibited by ERISA’s duty of loyalty. However, the preamble specifically notes that a “ESG” is one term used to describe certain non-pecuniary factors and that the meaning and terminology of the phrase itself continues to evolve.⁶ Thus, using this specific terminology in the Proposed Rule may be too narrow. We recommend that the final rule used the terms “pecuniary” and “non-pecuniary” investment factors or considerations. For example, paragraph (c)(1) could be amended to read:

(c)(1) Consideration of Pecuniary vs. Non-Pecuniary Factors. A fiduciary’s evaluation of an investment must be focused only on pecuniary factors. Plan fiduciaries are not permitted to sacrifice investment return or take on additional investment risk to promote non-pecuniary benefits or any other non-pecuniary goals. Pecuniary factors are those that present economic risks or opportunities that qualified investment professionals would treat as material economic considerations under generally accepted investment theories. The weight given to the various pecuniary factors should appropriately reflect a prudent assessment of their impact on risk and return. Fiduciaries considering factors that otherwise have broader non-pecuniary implications but which are, in fact, pecuniary factors are also required to examine the level of diversification, degree of liquidity, and the potential risk-return in comparison with other available alternative investments that would play a similar role in their plans’ portfolios.

We believe that this approach would allow the final rule to address future situations without the need for additional guidance to address new terms for ever-changing investment ideas and theories.

⁵ Even if not found liable, the mere fact that a technical foot-fault may have occurred is enough for a claim. Unfortunately, claims do not need to be legitimate to raise the risk of litigation liability, so something as simple as a documentation failure could subject to a plan sponsor to a claim that could result in litigation or, more likely, an expensive settlement regardless of the validity of the claim.

⁶ 85 Fed. Reg. at 39114.

The Department Should Remove the “All Things Being Equal” Approach from the Final Rule. The Department has requested comment regarding whether the “all things being equal” approach should be retained or abandoned, and on how “ties,” if they do exist, might be broken. We do not believe true ties exist because there are never two funds that completely identical except for ESG factors. For there to be a complete tie between two alternative investments, the alternatives would actually be one and the same investment. Even if, however, two alternatives could theoretically have the exact same risk and return profile such that they are economically indistinguishable, we believe a prudent fiduciary would consider investing an equal amount in each alternative. Financial theory would say that this would enable the fund to achieve the desired investment return at a lower overall level of risk because of the added diversification. Consequently, we recommend the elimination of paragraph (c)(2) and any reference to “economically indistinguishable investment alternatives.”

The Final Rule Should Eliminate the Prohibition of ESG Options or Components in Qualified Default Investment Alternatives (QDIAs). Paragraph (c)(3)(iii) explicitly prohibits the inclusion of ESG mandates or components in QDIAs. While we support pecuniary factors as being the paramount consideration for plan fiduciaries, the presence of ESG factors should not automatically deem an investment to be less prudent than an option that does not have an ESG component, and, thus, should not categorically prevent the option from being designated as the plan’s QDIA. This recommendation relates to our concern about the term “ESG” being used in place of “non-pecuniary” factors. A plan fiduciary could select a fund as a QDIA for purely pecuniary reasons but be prohibited from including it because there is an ESG component. Such a result is inapposite to the fiduciary principles stated by the Department and goes against ERISA’s history of not prescribing specific investment options for plan fiduciaries.

Comments Concerning Specific Language.

- Paragraphs (b)(1)(iii) and (c)(2) – A prohibition on incurring expenses to promote goals unrelated to the financial interests of plan participants and beneficiaries is appropriate and in keeping with the scope of these regulations. We recommend inserting the words “or expense” after the words “additional investment risk” in those paragraphs.
- Paragraph (c)(3)(i) – The term “benchmark” has grown to include such a broad array of investment measures that we believe it can no longer stand as an “objective risk-return criteri[on]” for use by fiduciaries in evaluating investment alternatives. For example, hundreds of benchmarks or indexes with ESG-oriented mandates in their composition now exists. We believe the word “benchmarks” can be deleted from the first line of this paragraph without detracting from the meaning.
- Paragraph (b)(ii) – The term “pecuniary factors” in this paragraph is followed by language that tracks the definition of that term contained in paragraph (f)(3) and is, therefore, superfluous.

Conclusion

Thank you for your consideration of our recommendations. We look forward to the opportunity to discuss them in greater detail or to answer any questions.

Sincerely,

A handwritten signature in cursive script that reads "Aliya Robinson".

Aliya Robinson
Senior Vice President, Retirement and Compensation Policy
The ERISA Industry Committee