# Comments on Department of Labor Pension ESG Rule

Richard Morrison

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At the end of last year, the Department of Labor (DOL) published a notice of proposed rulemaking seeking to rewrite rules on pension fund investing that were published by the previous administration. This new rule, "Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights," would overturn two similar existing rules and give pension fund managers greater leeway in using so-called environmental, social, and governance (ESG) factors in selecting investments on behalf of their beneficiaries. Private pension funds have long been regulated under the requirements of Employee Retirement Income Security Act (ERISA), which was passed in 1974 after a series of high-profile pension fund scandals and defaults by both corporate employers and labor unions.

I submitted a comment letter (blog post summary here) to the Department opposing the new rule, arguing that loosening the standard by which pension fund fiduciaries are allowed to operate would threaten the retirement security of millions of Americans and be inconsistent with the statutory requirements of ERISA. Many other interested parties also submitted comments with related objections, including many analysts and scholars that CEI has worked with in the past on related issues. Following are excerpts from several comments for readers interested in more detail on the topic. The Department of Labor is currently reviewing everyone's comments, and will likely publish a revised rule in the new few months.

**National Center for Public Policy Research's Free Enterprise Project**

Justin Danhof, Scott Shepard, and Sarah Rehberg

Fund managers must act without regard to partisan considerations. This proposed rule is an attempt to force them to act in favor of leftwing—and explicitly and exclusively leftwing—partisan considerations. It therefore misinterprets the underlying statute and is beyond the Department's authority to enact.
Were the Department, despite all of this, to enact this proposed rule, we hope and trust that it would be struck down in the courts. Were it to survive judicial review, then it would set the precedent for pension-fund managers to face the obligation to shift both their funds' investments and their voting procedures each time an incoming administration evinced a different partisan

outlook than the proceeding administration. After all, if this Administration is permitted to make pension-fund investing a hyper-partisan activity, then all future administrations must similarly be permitted to.
Full NCPPR comment here.

**American Enterprise Institute**

Benjamin Zycher

> The Prudence and Loyalty rule proposed by the Department of Labor cannot be made consistent with ERISA and the judicial decisions interpreting it, and thus with the fiduciary interests of participants in funds governed by ERISA, because the non-pecuniary factors proposed as investment objectives for such funds are immune to rigorous definition. They are, therefore, subjective, and thus inexorably political, inviting fund managers to substitute their political preferences to some degree in place of the fiduciary interests of plan participants as protected by ERISA. The "tie breaker" or "otherwise indistinguishable" model of non-pecuniary investment criteria cannot work as envisioned because analysis of future investment outcomes by definition is afflicted with important uncertainties, the resolution of which requires choices among alternative assumptions that cannot be quantified rigorously. They too are subjective and thus inexorably political.
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> A substantial body of evidence demonstrates that the insertion of non-pecuniary investment criteria in the management of pension and other such funds imposes a substantial penalty over time in terms of realized returns. This is not surprising: Such non-pecuniary criteria represent artificial constraints on investment choices and/or biases that interfere with the allocation of resources within a portfolio consistent with the various correlations and other investment characteristics that determine the financial outcomes yielded by fund performance. The data show that this is particularly the case for biases against investments in fossil-fuel sectors.

Full AEI comment here.

**FreedomWorks Foundation's Regulatory Action Center**

Beverly McKittrick and Alex Deise

> [T]he Biden Administration's Labor Department proposes to ignore ERISA's clear statutory dictate–investing retirement and pension funds solely to maximize benefits–and allow injection of so-called Environmental, Social, and Governance considerations into fiduciaries' decisions as to how to invest funds. This violates ERISA's fundamental principles of fiduciaries' duties of loyalty and prudence. It would also swing the door wide open for fiduciaries to insert their own political preferences in selecting investments, rather than being required to focus only on monetary returns.

> Investing to address ESG issues rather than to maximize returns is a growing trend among fiduciaries. Over the last few years, flows into these ESG funds have quadrupled. The problem is that often, these funds provide lower rates of return and charge higher fees. ESG investing may make investment managers feel like they are doing something "good" for society—but their idea of what's "good" is often to promote environmental extremism, social upheaval, and race and sex quotas for corporations. So not only does "woke investing" deprive Americans of retirement savings—it also supports beliefs that many do not agree with. So they'll have to delay retirement or get by on less money—so lely to advance a fiduciary's political agenda.

Full FreedomWorks comment here.

**Western Energy Alliance**

Kathleen M. Sgamma

**U.S. Oil & Gas Association**

Timothy Stewart

> Besides being outside the purview of ERISA, the time horizons of climate change simply do not match up with the time horizons of today's workers and pensioners. While it is widely recognized that a company or investment plan is more financially healthy when it does not sacrifice long-term performance for short-term gain, the time horizon invoked by the IPCC [Intergovernmental Panel on Climate Change] for which climate policy should be directed to ensure the temperature does not exceed 2 degrees Celsius of warming is 2100, while some government analyses looks to 2300. The year 2100 is so far into the future that it will not affect today's workers, including those just now embarking on their careers. Net-zero carbon by 2050 is a recent policy "innovation" on that long-term time horizon that is still too far into the future to justify sacrificing returns for today's workers. Financial regulation simply "cannot pretend to look past five years or so, and there is just no climate risk to the financial system at this horizon" except that introduced into the system by financial regulators themselves. …
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> We support the requirement in the current rule at paragraph (c)(2) that fiduciaries must "document why the selected investment was chosen based on the purposes of the plan, diversification of investments, and the interests of plan participants and beneficiaries in receiving benefits from the plan," when investments are determined to be "economically indistinguishable" under generally accepted investment theories and an ESG plan is chosen under the "tie breaker" principle. We support requiring plan managers to document the basis for determining that the chosen plan was indistinguishable in terms of risk-return parameters and hence, the selection of an ESG plan is appropriate. The documentation requirement is not an undue paperwork burden, as such information is normally documented by prudent investment managers. Further, this guards against subjective policy preferences predominating over the fiduciary responsibility to beneficiaries. To the extent that the documentation is a burden, it is a reasonable burden

> to guard against ERISA plan selections based on the policy preferences of managers that may not be shared by the beneficiaries.

Full WEA and USOGA comment here.

**Heritage Foundation**

David Burton

> The proposed rule contains both positive and highly negative provisions. At its core, however, it is an attempt to weaken ERISA's protection of plan beneficiaries to achieve political objectives that are unrelated to the purposes of ERISA in response to political pressure from the White House. To the extent that it is successful in achieving its objectives, the proposed rule will result in lower returns and less retirement income for plan beneficiaries. The DOL does not have the discretion to substitute its political judgement or that of the White House for that of Congress as expressed very explicitly by statute in ERISA.
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> The proposed rule is an invitation to ERISA fiduciaries to pursue their political or social goals at the expense of plan beneficiaries. Read honestly, the proposed rule would serve no other purpose. In effect, if the proposed rule were finalized, the DOL would be saying to plan fiduciaries "You must act in the interest of plan beneficiaries but if you pursue a progressive ESG objective at the expense of plan beneficiaries, we won't call you on it and, by the way, we have eliminated the means of actually enforcing the rules requiring that you act in plan beneficiaries' interests."
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> The proposed rule should be withdrawn.

Full Heritage comment here.

See also the podcast interview that the **Cato Institute**'s Jennifer Schulp did with Caleb Brown on "Labor Department, ESG, and Risks to Retirees."