

## **Comment Letter on the DOL's Proposed Rule On Investment Duties**

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My name is Ike Brannon. I am an economist and a senior fellow at the Jack Kemp Foundation as well as president of Capital Policy Analytics, a consulting firm in Washington DC. I was formerly an economist for the U.S. Treasury, the Office of Management and Budget, the Senate Finance Committee, the House Energy and Commerce Committee, and the Joint Economic Committee of Congress.

I am writing to support the Department of Labor's proposed investment duties rule, and I feel it is wholly appropriate for DOL to create clear regulatory guideposts to guide plan fiduciaries in matters of environmental, social, and government (ESG) investing.

I feel strongly about the necessity of preventing fiduciaries from being able to put their clients' money into funds that have an emphasis on achieving goals regarding environmental improvements, corporate government issues, or social welfare goals and averring that it is being done in the best interest of the people whose retirement dollars they are investing.

My last comment on a DOL rule was in the previous administration, when it set forth a rule [requiring](#) that a fiduciary always take steps that are in the best interest of the investor. A key argument the Administration made in support of that rule was the fact that even small deviations from this precept can cost investors a significant amount of their final retirement savings.

For instance, a study by the Obama Administration's Council of Economic Advisors [noted](#) that dismissing a reform simply because its aggregate

impact on the rate of return to retirement wealth is slight is disingenuous. It is relevant to the proposed rule, I believe.

Because of the miracle of compound interest, even small gains in returns can, over the three or four decades that a person saves for retirement, produce significant gains in wealth.

For instance, a 25 basis point reduction in earnings over a lifetime of retirement savings because of portfolio choices to achieve non-pecuniary investment goals can reduce the wealth of an investor by nearly ten percent at retirement. Pretending that such a diminution in returns, sacrificed to pursue an ostensibly noble social goal, represents a minor cost to the investor, is simply not correct.

Foisting such investment decisions on a worker who is saving for retirement can impact returns in two different ways. For starters, constraining a portfolio to leave out a sizable class of stocks means that it will be less likely to match the performance of the stock market as a whole. This is especially true if we were to eliminate gas and oil producing companies from a portfolio. Since these stocks tend to be less volatile and pay a significant and dependable dividend--even when demand has been destroyed and supply is nearly unconstrained as is the case today--it means that removing such low-volatility stocks results in a portfolio that's more volatile without necessarily any commensurate increase in returns. That is, they're accepting more risk without more reward.

The second problem with self-imposed mandates on socially and environmentally conscious investing is that the management fees for such investment vehicles tend to be quite a bit higher than index funds, since there need to be conscious choices made as to what, precisely, should belong in the fund. A 2020 Morningstar report [suggests](#) that passively-managed ESG funds have a fee about .1% higher than non-ESG stock index funds.

## The Difference Between ESG and Index Fund Expense Ratios

Firm	Index	ESG Index	Difference
Fidelity	.00%	.11%	.11%
Vanguard	.04%	.12%	.08%
Blackrock	.0125%	.18%	.1675%
State Street	.01%	.26%	.25%
TIAA	.04%	.35%	.31%

It's also not correct to go a step farther, as many of the proponents of environmental, social, and aver that these issues are so important that investors would welcome the tradeoff.

An investor who is concerned about the environment, or about broader social justice issues or the corporate governance matters at a particular firm, has the means and ability to express himself if he or she so chooses to do, whether it be by donating money to charities that engage in such issues, voting for politicians who espouse such perspectives, or consciously investing some of his wealth in such a way so that it furthers his non-pecuniary goals. But doing it on his behalf, and insisting that he benefits from that, is simply disingenuous and represents an act done for the interests of the fund manager, contradicting his fiduciary responsibilities.

Some fiduciaries aver that socially responsible investing does not, in fact, cost its investors a dime, because the suite of stocks that qualify for such treatment are better poised to prosper in future. They argue that, essentially, the market has collectively mispriced such stocks. Again, I beg to differ. Excluding a broad swath of the stock market from a portfolio--a decision that discounts an entire sector of the economy and also applies

somewhat arbitrary standards elsewhere--is by no means a recipe for greater investment success.

Despite what we might fervently wish to be the case, it is almost assuredly the case that we will still be consuming oil and natural gas for the next couple of generations at a minimum. Companies that can efficiently extract these fuels from the ground have performed quite well in the stock market over the past few decades, notwithstanding the unique situations in the energy market today that's left supply expanding while demand evaporating overnight.

Doing without these sectors in a portfolio will, in all likelihood, reduce its long-term performance. The market has already discounted its best guess as to the long term changes in supply and demand and incorporated it into its stock price. Assuming it has made some sort of systematic mistake, and attempting to capitalize on it, is of course the province of any activist investor, but that's not what should be done on behalf of people who regularly contribute a portion of each paycheck into the retirement account.

People can invest their own money as they see fit. But fiduciaries cannot use their social preferences to guide their investment choices or pretend that by doing so that it benefits those for whom they invest.