Received: July 28, 2020
Tracking No. 1k4-9i2n-i7dj
Comments Due: July 30, 2020
Submission Type: Web

PUBLIC SUBMISSION

Docket: EBSA-2020-0004
Financial Factors in Selecting Plan Investments

Comment On: EBSA-2020-0004-0002
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Document: EBSA-2020-0004-DRAFT-0707
Comment on FR Doc # 2020-13705

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General Comment

I am an economic policy advisor who works with U.S. and global clients.

The Employee Retirement Income Security Act (ERISA) requires accountability and places fiduciary obligations on those with discretionary control or management responsibilities for retirement plans. This includes seeking to ensure that they act in good faith to maximize financial returns over time.

Today, the challenge of ensuring retirement security for Americans remains. A prolonged period of low interest rates created a complex investment environment. Nothing should distract managers of ERISA retirement plans from a single-minded focus on maximizing the financial value of the assets they manage. Allowing fiduciaries to substitute or even supplement ESG (environment, social and governance) goals for financial returns does a disservice to those who are counting on these funds in retirement.

After all, what is a retirement fund for?

It is a pooling together of pension and/or other retirement contributions that are invested with a view to securing an increase in their financial value over time. Higher returns give contributors more money to live on in retirement, which is the singular purpose of these funds in the first place. Significant deviations from a focus on returns can lead to solvency problems for funds over time.

The idea of "socially responsible" investing has a long history in the United States and there are numerous funds that are responsive to different ESG considerations. Individuals are perfectly free to invest their money in any of these vehicles. If these investment vehicles deliver sub-optimal financial returns, those investing in them are presumably fine because non-financial considerations were addressed along with financial ones.

The challenge arises when ESG considerations are introduced in the investment calculus of fiduciaries overseeing federally regulated retirement funds. How so?

Proponents of a broad mandate of ESG considerations often point to research that argues that including these considerations leads to better returns. How can one broadly assert that an ESG centric investment strategy is better when there is no common definition of what is included in each bucket?

The Motley Fool article "What is ESG Investing?" by A. Lomax and J. Rotonti, Feb. 25, 2020 does a good job setting forth an indicative list. Under "E", for example, topics include:

- Climate change policies.
- Greenhouse gas emissions goals.
- Carbon footprint/intensity.
- Water-related issues/goals.
- Renewable energy usage.
- Recycling/safe disposal practices.
- Green products/technologies/infrastructure.
- Environmental benefits for employees.
- Relationship/history with environmental regulatory bodies.

Unlike, say, the LEED standard for buildings, which has an accepted scoring methodology, no such framework exists for determining that environmental plan X is better than plan Y. There is also no agreed certifying body that ensures that companies "worthy" of receiving "ethical" capital are actually living up to their stated practices.

Then there are definitional challenges with application. Hydropower, for example, has divisive in debates around state renewable energy standards. Some see it as green energy - clean water rolling over a turbine. Others focus on the impact of dams.

While credibly asserting that ESG strategies lead, broadly speaking, to better returns is impossible, we can be certain that it introduces greater complexity in the fund management process. This complexity undoubtedly diminishes the focus of maximizing financial returns.

Separately, is it ethical for fiduciaries to introduce ESG into their investment strategies? Those who contribute to retirement funds, either directly or through an agreed employer contribution, are doing so on the idea that the fund manager will work to maximize financial returns. Any deviation from that mission would represent a departure from the core premise of the contribution.

Would ESG plans that help guide investment strategies for ERISA-accredited retirement funds create risks or costs for the Pension Benefit Guaranty Corporation (PBGC)? The level of risk may be variable, depending on the extent and skill to which ESG factors are applied. Yet, drawing on the U.S. Government backstop to promote approaches or values that are not universally agreed or legally required seems questionable.

In the final analysis, the proposed regulatory changes should be supported. The goal of maximizing returns to provide contributors with greater income in retirement is important enough that the PBGC was established to insure these plans against the risk of failure. The public guarantee is made and justified on the assumption that fiduciaries will do their part.

Let people do what they wish with their money. For publicly regulated/ guaranteed retirement funds, ESG has no place in the investment mix, except--as the regulation makes clear--when the economic returns are "indistinguishable."