IMPAX Asset Management
Adviser to Pax World Funds

November 22, 2021

Fred Wong
Acting Chief of the Division of Regulations
Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Avenue NW
Washington, DC 20210
Attention: Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights

Dear Mr. Wong,

I am writing on behalf of Impax Asset Management LLC in support of your new proposed rule, Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights. Impax Asset Management is an asset manager with more than $50 billion in assets under management. We seek to generate superior, risk-adjusted investment returns on behalf of our clients and shareholders by investing in companies we believe are better positioned to seize the opportunities and mitigate the risks associated with the transition to a more sustainable economy. In doing so, we integrate ESG research and analysis into all our investment portfolios.

We believe that the proposed rule corrects the deeply flawed provisions of two previous rules issued in 2020 — Financial Factors in Selecting Plan Investments and Fiduciary Duties Regarding Proxy Voting and Shareholder Rights.

Materiality and Unequal Treatment

We commend the Department for abandoning the use of the term "pecuniary," which has no precise meaning in connection with fiduciary duty, and for focusing instead on "materiality," a concept that is of course familiar to investors. Indeed, it is central to investing, and is defined in regulation and law. The "pecuniary" vs. "non-pecuniary" construct under the previous rule was nothing more than a rather clumsy attempt to establish a separate standard unique to ESG funds and ESG factors, which would not be equally applied to other investment funds or factors, the object of which was simply to exclude ESG funds and factors from consideration in retirement plans. Materiality, on the other hand, is not only an accepted financial concept that investors and companies are deeply familiar with, but there is also a great deal of reliable evidence from financial and academic studies underscoring significant links between ESG factors and financial outcomes. These studies not only clearly show that funds incorporating ESG do not sacrifice risk-adjusted returns, but perhaps more importantly, that there is often a correlation between ESG factors and financial risk and performance over the medium to long term.

As Morgan Stanley has pointed out, "…funds incorporating environmental, social and governance (ESG) criteria can potentially provide financial returns in line, if not better than, traditional funds, and with less downside risk."[1] RBC said much the same in 2019: "The main finding from this updated body of work remains that socially responsible investing does not result in lower investment returns."[2] ThinkAdvisor noted, "In the first quarter of 2020, 70% of sustainable equity funds **finished in the top halves** of their Morningstar categories, and 24 of 26 ESG-tilted index funds outperformed their closest conventional counterparts. BlackRock found that 94% of sustainable indexes outperformed during that time. Findings from MSCI and S&P found similar results."[3]

There is clearly no *fiduciary* rationale for singling out ESG funds for burdensome scrutiny and automatic exclusion from retirement plans. The invention of "pecuniary" as a financial concept may have been an attempt to accomplish the same, but we are encouraged to see the Department has now rejected that approach.

Not only did the previous rule ignore hundreds of empirical studies underscoring the materiality of ESG factors, but it strains credulity to think that the record inflows[4] into ESG investments over the past few years would have materialized had risk-adjusted performance been inferior.

Innovation

Efficient financial markets must, of necessity, adapt to changes in the world economy, as must fiduciaries if they are to deliver competitive risk-adjusted returns to retirement plan participants. When ERISA was written in 1974 climate change wasn't on anyone's agenda outside a small section of the scientific community. The world has changed. Losses from natural catastrophes since 1974 have gone up by two orders of magnitude, and while not all natural catastrophes are linked to climate change, many are, including floods, fires, tropical cyclones, sea level rise, and heat. Thus, losses and the risk of loss associated with climate-related disasters have become material risks to companies and investors, something financial markets and fiduciaries must account for. They are doing so, in part, by integrating climate-related risks

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[1] Morgan Stanley Institute for Sustainable Investing, "Sustainable Reality: 2020 Update," 2020. 3190436-20-09-15_Sustainable-Reality-2020-update_Final-Revised.pdf (morganstanley.com)

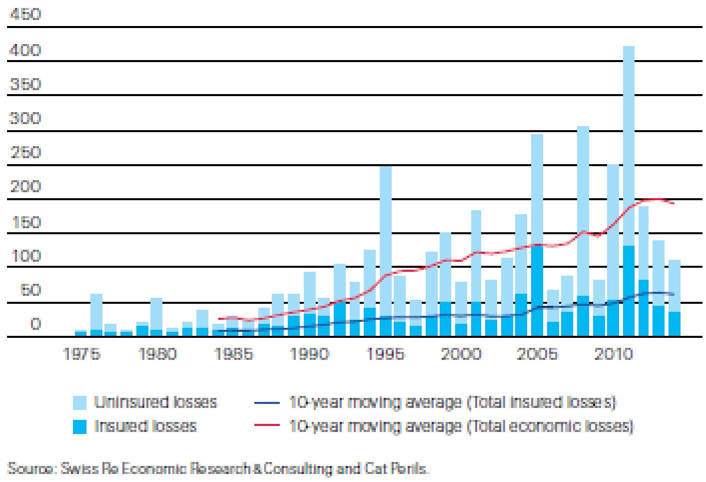
[2] RBC Global Asset Management, "Does socially responsible investing hurt investment returns?" 2019. does-socially-responsible-investing-hurt-investment-returns.pdf (rbcgam.com)

[3] Kiley Miller, "Sustainable Investing Doesn't Mean Sacrificing Returns," *ThinkAdvisor*, July 17,2020. Sustainable Investing Doesn't Mean Sacrificing Returns | ThinkAdvisor

[4] See, for example, Patturaja Murugaboopathy and Simon Jessop, "Global sustainable fund assets hit record $2.3 tln in Q2, says Morningstar," Reuters, July 27, 2021; Jon Hale, "A Broken Record: Flows for U.S. Sustainable Funds Again Reach New Heights," Morningstar, Jan. 28, 2021; and Pippa Stevens, "There's no hotter area on Wall Street than ESG with sustainability-focused funds nearing $2 trillion," CNBC, April 30, 2021.

and opportunities into investment portfolios, and there is no reason why such portfolios should be unavailable to retirement investors.

Natural catastrophes losses 1975-2014, $billion



Source: Swiss Re, "Underinsurance of property risks: closing the gap," No5/2015. [swiss re underinsurance of property risks-closing the gap.pdf]

The same is true of many other issues. Cybersecurity was not on the risk radar in 1974, but it is a material risk that companies and investors need to pay attention to today. As Natixis pointed out in its original comment letter to DOL on the rule adopted last year, "the Department resisted calls to identify specific investment products as QDIAs because doing so would cause them to be fixed at a certain point in time rather than '…accommodate future innovations and developments in retirement products.'"[5] The best investment practices are those that adapt to changing economic, social and financial landscapes, and in today's global economy, ESG factors can help investors better understand those landscapes.

Shifting Guidance

We would note the Department has acknowledged that shifting interpretations of fiduciary duty with respect to ESG or sustainable investment funds has created confusion and a chilling effect for ERISA plan fiduciaries in selecting funds. While the new proposed rule is far better documented and more sound than the rules it replaces, it may not end the confusion if a future administration chooses to take a different approach. In this regard, we commend the Department for noting that including ESG factors that are material is something that is not only permitted under fiduciary duty but *required*.

[5] David L. Giunta and Edward Farrington, Comment Letter on RIN 1210-AB95 – Financial Factors in Selecting Plan Investments," Natixis Investment Managers, July 30, 2020. 00563.pdf (dol.gov)

That idea has been discussed for nearly two decades, at least since the publication of the first Freshfields Report in 2005, a report about the requirements in nine countries[6] regarding the ability to integrate ESG factors into investment under each country's definition of fiduciary duty.[7] The report concluded:

> "Conventional investment analysis focuses on *value*, in the sense of financial performance. As we note above, the links between ESG factors and financial performance are increasingly being recognised. On that basis, integrating ESG considerations into an investment analysis so as to more reliably predict financial performance is clearly permissible and is arguably required in all jurisdictions."

A follow-up Freshfields paper in 2009 provided a sequel to the original report, including a legal roadmap for fiduciaries looking to operationalize their commitments to responsible investment.[8] A third report, produced by UNEP Finance Initiatives, followed up on the two Freshfields reports and reinforced their findings, noting that "Failing to consider long-term investment value drivers, which include environmental, social and governance issues, in investment practice is a failure of fiduciary duty."[9]

Essentially, this is the position the Department has now taken, which we applaud. We strongly support adoption of the new proposed rule.

Tiebreakers

While we would be supportive of adding flexibility to the previous rule's tie-breaker provision, which allowed fiduciaries to "focus on the collateral benefits of an investment or investment course of action to decide the outcome", we would strongly urge instead that the Department drop all reference to tie-breaker provisions or explanations. The notion of a "tie" between investment options necessitating some sort of "tie-breaker" test or process is absurd on its face. Fiduciaries are accustomed to deliberating on such matters, including close calls, and if they are doing their job and creating an appropriate record there should be no need for "tie breaker" guidance in the rule. Indeed, the proposed rule already notes that existing disclosures should be "sufficient to satisfy the disclosure element of the tie-breaker provision." In that case, it makes little sense to include that provision at all.

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[6] These countries include Australia, Canada, France, Germany, Italy, Japan, Spain, the United Kingdom and the United States.

[7] Freshfields Bruckhaus Deringer, "A legal framework for the integration of environmental, social and governance issues into institutional investment," UNEP FI, October 2005. A legal framework for the integration of environmental, social and governance issues into institutional investment : October 2005 (unepfi.org)

[8] Freshfields Bruckhaus Deringer, "Fiduciary responsibility: Legal and practical aspects of integrating environmental, social and governance issues into institutional investment,: UNEP FI, 2009. fiduciaryII.pdf (unepfi.org)

[9] UNEP FI, "Fiduciary Duty in the 21st Century," 2015. download (unpri.org)

Additional Examples

Finally, the revised rule provides several examples of ESG factors that are widely considered material to investment decisions, including climate change, governance, and workforce practices. We appreciate that the Department takes a broad view of what factors might have materiality, and that additional ESG factors not specifically named in the proposed rule may be considered material as well. In answer to the question in the proposed rule about providing additional examples, we would urge that the Department not try to provide an extensive list of examples but to continue to reinforce the point that the examples already noted in the proposed rule are *only* examples. There are more examples, many of which are included one or more of the 400+ individual papers that we provided in our comment letter on the ERISA rule last year. We would particularly note the extensive literature on the impact of diversity in decision-making bodies such as boards and management.

Thank you again for your thoughtful work.

Sincerely,

Joseph F. Keefe
President
Impax Asset Management LLC

Julie Gorte
SVP for Sustainable Investing
Impax Asset Management LLC