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VIA ELECTRONIC FILING

Office of Regulations and Interpretations
Employee Benefits Security Administration Room N-5655
U.S. Department of Labor
200 Constitution Avenue, N.W.
Washington, D.C. 20210

RE: ***Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights***

Attention: RIN 1210-AC03

Dear Acting Assistant Secretary Khawar,

I respectfully write in support of and to provide comments on the Department of Labor's (Department's) proposed rule, *Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights* (the Proposed Rule), 86 Fed. Reg. 57272 (Oct 14, 2021).

I have spent the last 28 years as a legal scholar studying benefit plan regulation, particularly with respect to fiduciary duties. Earlier in my career, I worked in human resources at a large plan sponsor and worked in the employee benefits practice of a large law firm. My professional opinion is that the core provisions of the Proposed Rule are imperative to protect the security of U.S. workers' pensions. Below, I offer some general comments, then outline the important advancements made by the Proposed Rule, and finally respond to some of the Department's requests for comments.

Overview

When read carefully, at its heart the Proposed Rule makes clear that ERISA's fiduciary obligations of prudence and loyalty apply to all investment-related decisions. The Department's guidance on investment decisions and the exercise of shareholder rights consistently has been and remains, at its core, that fiduciaries must act prudently and in the best of interest of the plan and its participants and beneficiaries. Over more than 40 years, the Department has

provided formal and informal guidance on how fiduciaries should integrate various factors during the investment decision-making process, make decisions among investments that are equivalents in terms of risk and reward, and exercise shareholder rights. While the core standards of prudence and best interest never varied, the accumulation of guidance and changes in its tone created confusion among fiduciaries. The Proposed Rule eliminates any uncertainty as to whether there are favored or disfavored factors that fiduciaries must or should use when making investment decisions and exercising shareholder rights. It clearly allows fiduciaries to consider all relevant information and places the burden in identifying what information that is for any given investment-related decision or exercise of shareholder rights squarely where the burden belongs – on the fiduciaries that have the decision-making responsibility.

Some commentators may allege that the Proposed Rule does a disservice to retirement savers by singling out environmental, social, and governance (ESG) factors as favored factors. The Proposed Rule does no such thing. The preamble discusses the history of the Department's guidance on ESG factors and the chilling of the use of those factors that resulted. The Proposed Rule itself does not single out ESG factors, other than to provide comfort to fiduciaries that they are permitted to consider relevant ESG factors just as they may consider any other relevant factors. Specific reference to ESG factors and use of ESG-related examples are important in order to clarify what strong evidence shows to be a misunderstanding or lack of clarity among fiduciaries responsible for ERISA plan investments about the use of those factors.

Other commentators may argue that consideration of ESG factors is imprudent either because it is incompatible with the efficiency of markets or because those factors are too ill defined and trendy to have met the test of time required for prudence. Both arguments are wrong. The argument on efficient markets proves itself to be incorrect. Efficient market theory contends that sophisticated and knowledgeable investors will identify and invest in mispriced assets. Those investments correct market inefficiencies. The incentive for investors to undertake the costs involved in identifying mispricing is their ability to earn above market returns. If ESG factors are relevant, then the only way market prices reflect them is by investors that exploit existing inefficiencies. To the extent that some markets are inefficient, mispriced assets offer even greater opportunity for gains. Mispriced assets may not be a prudent investment for all plans. No rationale, though, supports a declaration that it is per se imprudent for fiduciaries to invest in assets they belief to be mispriced. In addition to the negative effect on plans, putting trillions of dollars of pension plan capital on the sidelines would increase inefficiencies in the capital markets.

The other argument – that the use of ESG factors is a misguided trend like tulip mania in the 17th century or that ESG factors are too vague and ill defined to be prudent – also fails. Tulips are a commodity. Temporary demand that outstrips supply and speculation may drive up the prices of tulips, Beanie Babies, bottled water during a hurricane or other goods to levels that cannot be supported once demand drops or supply increases. However, analysis of the risks

and rewards of, for example, climate change differs in kind, not just in degree from that type of speculation in goods.

It is true that, for example, the evaluation of climate change risk is evolving. Climate change experts do not agree on the specific assumptions, interpretations of less than transparent disclosures, or scope of data to be used to predict the physical and economic risks of climate change. That does not mean, though, that it is per se imprudent for fiduciaries to analyze and price the expected impact of climate change on assets. Investors who engage in superior analysis will achieve better long-term results than those who rely on weaker analysis. That is in the nature of markets and investments. Risk resulting from difficult-to-evaluate future outcomes is neither new nor limited to ESG factors. Consider investments in early stage pharmaceutical research. Some scientists may conclude that a company's stream of research is likely to lead to the creation of an important new vaccine; others may conclude that is unlikely. The difference in analysis should not mean that an investment in the company would be per se imprudent. It is for fiduciaries to decide, based on appropriate consideration of the relevant facts and circumstances, whether the investment is prudent and appropriate given the plan's entire portfolio.

Contributions of the Proposed Rule

The following points identify some of the important advancements made by the Proposed Rule.

First, the Proposed Rule makes clear in b.1.i. that a fiduciary acts prudently if she gives "appropriate consideration to those facts and circumstances that . . . are relevant" either to the specific investment or to the role of the investment in the portfolio. The language clarifies that the Department has not moved away from its historical and core position that ERISA fiduciaries have the discretion necessary to make prudent investment decisions based on whatever factors, without exclusion, are relevant to those decisions.

Second, in b.2.ii.C. the Proposed Rule explicitly includes "the economic effects of climate change, and other environmental, social or governance factors" as factors that the fiduciary "often" will be required to evaluate as part of making a prudent decision. This eliminates any remaining questions on whether these factors are among those that may be important as part of a prudent decision making process. The current language has the benefit of allowing for the exceptional circumstance where those factors clearly are not relevant.

Third, the Proposed Rule is consistent with the Department's long-held position on ERISA's core duty of loyalty. In c.1. it states that a loyal fiduciary is not permitted to "promote benefits or goals unrelated to interests" of the plan or the participants and beneficiaries. At the same time, it reminds the fiduciaries of two important corollaries. The fiduciary must evaluate plan investments "using appropriate investment horizons." This typically means using a long-term

horizon. Moreover, climate change, governance, and workforce practices, are among the factors that may be part of a loyal fiduciary's analysis.

Fourth, although the text of the Proposed Rule appropriately does not explicitly refer to Qualified Default Investment Alternatives, the preamble states that the fiduciary standards in the Proposed Rule apply to decisions on QDIAs. QDIAs play a particularly important role in US retirement savings because a significant portion of defined contribution plan assets are invested in QDIAs. When read in conjunction with the preamble, by not calling out QDIAs, the Proposed Rule calls for the consistent application of the core ERISA principles of prudence and loyalty to fiduciary decisions on QDIAs and other investment-related decisions.

Other Comments

The following points engage with specific provisions on which the Department solicited comments.

b.2.i. This provision essentially restates ERISA's prudence provision as applied to investment decision making. As such, it is unnecessary. Some might read its inclusion as an intent to change the current application of the general concept. For example, the preamble to Investment of Plan Assets Under the "Prudence" Rule, 44 Federal Register 37221 (1979) indicated that some commentators feared the rule might be read to impose extensive and expensive systems to engage in comparative analysis on all plans regardless of factors such as plan asset levels. The Proposed Rule can avoid creating any similar concerns by eliminating b.2.i.

b.4. The examples in this provision are both sufficient and appropriately neutral. They address the factors that have recently been the subject of some ambiguity as to whether it is prudent to consider them. Although other commentators might suggest the addition of other factors, such as the quality of a company's products or a compelling strategy for expansion, such additions are unnecessary. To my knowledge, no one has ever seriously proposed that it would be imprudent or disloyal for a fiduciary to consider product quality or important strategic plans. It would be impossible to list all the factors that might affect a prudent investment decision, so where would such a list end? At some point, even with the "for example" language that introduces the list, a long list might create an inference that it is exclusive or that a fiduciary always needs to consider all of the listed factors. I support the language as proposed.

c.3. The first sentence of c.3. in the Proposed Rule provides important clarification that a fiduciary may consider collateral benefits in what have become known as tie-breaker situations.

The rest of the language in c.3. should be deleted. Other than in limited situations involving employer securities, ERISA does not impose different fiduciary obligations based on the type of

investment involved. The Department should not single out any specific types of investment decisions for different regulatory treatment. In the case of a tie-breaking decision made based on collateral benefits, imposition of a disclosure requirement could discourage plan fiduciaries from making decisions based on factors that are both prudent and loyal. As the Department noted in the preamble to the Proposed Regulation, a comparison of potential investments may reveal that multiple investments with very different attributes are equivalent in terms of the role they would play in the plan's portfolio. In making a choice among those investments, a plan fiduciary's decision should be subject to ERISA's normal requirements of prudence and loyalty, no more and no less.

Some commentators seem to misapprehend the core of ERISA's fiduciary duty of loyalty and its application to tie-breaker situations. The Supreme Court has looked to trust law to inform ERISA's definition of loyalty, but has recognized that trusts and ERISA plans are not equivalents. In both trust law and employee benefits law, the duty of loyalty discourages fiduciaries from engaging in opportunistic behavior vis-à-vis the trust's beneficiaries or plan's participants and beneficiaries. The obligation is adapted in benefit plans, though, because unlike in trusts fiduciaries are permitted to have conflicts of interest.

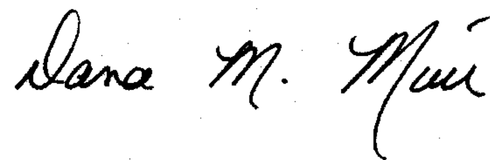
The Supreme Court has held that loyal fiduciaries must act in the financial best interest of the plan and its participants and beneficiaries. In tie-breaker situations, it is an unwarranted leap to conclude that the duty of loyalty necessarily always precludes fiduciaries from considering any other interests. The fiduciary culled opportunities based on the plan's and participants' and beneficiaries' best interests before identifying the investments that are equivalents. Thus, the fiduciary met its obligation under the best interest standard.

After meeting the financial best interest standard, when making a decision among equivalent investments, the fiduciary remains bound by loyalty and prudence. The fiduciary cannot make a decision that would benefit itself without violating its obligation of loyalty. Nothing in ERISA fiduciary law, though, is inconsistent with the fiduciary choosing an investment at that point that provides collateral benefits to the plan, or to the plan's participants and beneficiaries. Arguably, ERISA's "best interest" language even requires a decision be made on factors that benefits the plan, participants, or beneficiaries rather than making a decision by a random action such as a coin flip.

If the Department believes it is necessary to provide guidance after the first sentence of c.3., I propose language such as: "A decision between such investments is subject to the requirements of ERISA Sections 404(a)(1)(A) and 404(a)(1)(B)."

Thank you for the opportunity to comment on the Proposed Rule. It will ensure that ERISA's core fiduciary provisions are applied. It will confirm fiduciaries are able to consider all available information in making investment decisions and understand their obligation to act prudently and loyally in the exercise of shareholder rights. I appreciate the Department's hard work, analysis, and diligence in drafting this important Proposed Rule.

Very truly yours,



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