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Mr. Ali Khawar
Acting Assistant Secretary of Labor
Office of Regulation and Interpretations
Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Avenue NW
Washington DC 202010

Re**:** Comment on Rulemaking – **RIN1210-AC03**
**Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights**

Dear Mr. Khawar:

We appreciate the opportunity to comment on the Department's proposed rule on ESG investing and proxy voting, *Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights*. Overall, we believe the proposed rule will ensure fiduciaries are permitted to select from a wider pool of investment strategies with the greatest potential to generate risk-adjusted competitive financial returns. We also support the provisions on proxy voting that reaffirm the Department's long-standing position that fiduciaries should ensure proxy votes are cast in the best interest of plan participants. We applaud the work underpinning the proposed rule and expect the final rule will help fiduciaries prioritize financial return by assessing all relevant factors that impact investments.

We support the Department's view that, "…material climate change and other ESG factors are no different than other "traditional" material risk-return factors…" The length of time for which a factor must exist to be deemed traditional is unclear. What is clear is that ESG factors are a way to capture inputs that have long been and, in many cases, continue to be unaccounted for in corporate accounting.

Risks from climate change and other systemic factors also impact investments. Phillips 66, for example, recently wrote down $1.3 billion in its third quarter earnings report after Hurricane Ida severely damaged its New Orleans-based Alliance Refinery. As a result of these write downs, press reports indicate more than 400 people are likely to lose their jobs. The episode further supports the need to prepare for climate change-related risks. It also shows that climate risks also threaten quality jobs. Investor focus on ESG risks will incentivize companies to provide more fulsome disclosure. Companies reporting on their progress on the climate transition should also be reporting on how the transition will impact decent work and quality jobs, a concept known as Just Transition.

Similarly, poor human capital management policies for front line workers amidst the outbreak of the Covid-19 pandemic posed operational risks and yielded disproportionate impacts on people of color. A focus on material ESG factors may prevent such trends from repeating.

Several studies cited in the proposed rule support the value proposition of ESG. A contrary study cited in the proposed rule that found ESG had a lower return over a ten-year period was flawed in its methodology.[1] The study evaluated multiple actively managed ESG funds that were not randomly selected compared to a passive index when it should have compared ESG funds to other active managed large cap equity funds, which also struggled to beat the passive index over the same ten-year time period. The study fixated on expense ratios even though actively managed funds charge a premium relative to passively managed funds regardless of ESG characteristics.

The Department outlined three examples of ESG issues that a fiduciary may consider in the evaluation of an investment or investment course of action if material, including: "(i) Climate change-related factors, such as a corporation's exposure to the real and potential economic effects of climate change, including its exposure to the physical and transitional risks of climate change and the positive or negative effect of Government regulations and policies to mitigate climate change; (ii) governance factors, such as those involving board composition, executive compensation, and transparency and accountability in corporate decision-making, as well as a corporation's avoidance of criminal liability and compliance with labor, employment, environmental, tax, and other applicable laws and regulations; and (iii) workforce practices, including the corporation's progress on workforce diversity, inclusion, and other drivers of employee hiring, promotion, and retention; its investment in training to develop its workforce's skill; equal employment opportunity; and labor relations."

We agree the above-named factors may have a material impact on investments. We also agree with the Department that additional ESG factors not mentioned in the proposed rule should also be considered if they are material to investing. We urge the Department to maintain the full list of factors mentioned in the proposed rule and to consider adding the CEO to median worker pay ratio as well.

The CEO to median worker pay ratio provides investors with an important indicator of human capital management and is a logical extension of the items listed under (iii) pertaining to the work force. The pay ratio is required reporting under SEC regulations and therefore investors can access the public information consistently across U.S. registered firms.

Additional ESG risks and opportunities will continue to be identified and refined as quality reporting improves over time. Therefore, above all else we implore the DOL to make clear that any list of ESG factors in the body of the rule is not exhaustive.

[1] Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, Proposed rule, Oct. 14, 2021, available at: https://www.federalregister.gov/documents/2021/10/14/2021-22263/prudence-and-loyalty-in-selecting-plan-investments-and-exercising-shareholder-rights, page 57291, see "For example, Winegarden shows that over ten years, a portfolio of ESG funds has a return that is 43.9 percent lower than if it had been invested in an S&P 500 index fund."

A return to the tie-breaker standard in which collateral benefits may be considered is a more feasible approach than the current regulation's specific documentation requirements. The prohibition on fiduciaries accepting lower returns or additional risk to secure a collateral benefit will ensure the focus is on the materiality of ESG factors. We support the tie-breaker standard as outlined in the proposed rule and do not believe additional specificity is needed. Fiduciaries are already required to make investment decisions in the best interest of plan participants and the consideration of collateral benefits should not require a unique assessment of participants' views.

More specificity would be helpful on another aspect of the proposal. The proposal would require in the case of a designated investment alternative for an individual account plan the plan fiduciary must ensure that the collateral-benefit characteristics of a fund, product, or model portfolio, including for a QDIA, should be prominently disclosed to participants and beneficiaries. An example of model disclosure would be helpful to assist with compliance.

We support the removal of the two safe harbors for proxy voting policies, which we viewed as problematic as outlined in our previous comment letter to the Department.[2] We also support the removal of a documentation requirement on the decision-making of whether to exercise proxy voting rights. As explained in our prior comment letter, these requirements increase the costs of proxy voting and would likely discourage fiduciaries from casting votes on impactful ESG issues.

The proposed rule maintains that an investment manager must vote proxies in a pooled vehicle in proportion to each plan's economic interest in the vehicle. Investment managers face an operational challenge given that they do not typically vote pooled vehicles proportionally, although that may change going forward. We support the alternative option of an investment manager sharing a proxy voting policy that participating plans are required to accept prior to investing in the vehicle.

We appreciate the opportunity to share our perspective.

Sincerely,

John DeMairo
President
Chief Executive Officer

Maureen O'Brien
Vice President
Director of Corporate Governance

[2] Segal Marco, October 5, 2020, accessed at https://www.regulations.gov/comment/EBSA-2020-0008-0267.