



FEDERAL RETIREMENT THRIFT INVESTMENT BOARD

77K Street, NE Washington, DC 20002

May 13, 2022

VIA ELECTRONIC SUBMISSION

Attention: Request for Information on Possible Agency Actions
Office of Regulations and Interpretations
Employee Benefits Security Administration, Room N-5655
U.S. Department of Labor
200 Constitution Avenue NW
Washington, DC 20210

Re: Z-RIN 1210-ZA30, Request for Information on Possible Agency Actions to Protect Life Savings and Pensions from Threats of Climate-Related Financial Risk

Dear Sir or Madam:

I appreciate the opportunity to comment on the U.S. Department of Labor's ("DOL") Request for Information on *Possible Agency Actions to Protect Life Savings and Pensions from Threats of Climate-Related Financial* ("RFI").

The FRTIB is a Federal agency that was established in 1986 by the Federal Employees' Retirement System Act of 1986 (FERSA)¹. The FRTIB administers the Thrift Savings Plan (TSP)—a retirement savings plan for federal civilian employees and members of the uniformed services that is similar to private-sector 401(k) plans. The FRTIB is managed by a Presidentially-appointed five-member Board and an Executive Director chosen by the Board to manage the day to day operations of the Agency. As the FRTIB's Executive Director, I am responsible for interpreting and implementing most of the FERSA provisions relating to TSP administration.²

Background

- The TSP is the world's largest defined-contribution plan. As of March 31, 2022, we hold \$762 billion in trust on behalf of 6.5 million participants. Although the TSP is administered by a government agency, the funds we hold in trust are not government funded or government owned. The funds consist of contributions by participants of money to which they have pre-existing property rights, and those contributions are recorded as such in accounts

¹ Public Law 99 335, 100 Stat. 514. The provisions of FERSA that govern the TSP are codified, as amended, largely at 5 U.S.C. 8351 and 8401-79.

²See 5 U.S.C. 8474.

maintained separately for each individual. In this respect, the TSP is very different from most large government pension plans and sovereign wealth funds.³

There are special risks inherent in the Federal government's administration of such a large pool of *private* savings. For example, FERSA's legislative history is brimming with Congressional concern over the risk that the executive branch of government will pressure TSP-fiduciaries to engage in market manipulation or subordinate loyal stewardship of TSP funds to constantly changing national policy priorities. The House and Senate Conference Committee "spent more time on this issue than any other."⁴ As a result, FERSA contains a handful of provisions specifically designed to address conflicts of interest that are unique to the peculiar relationship between the executive branch and TSP participants.

Congress addressed these special risks by significantly restricting the FRTIB's (and, by extension, the executive branch's) discretion to make investment-related decisions. Congress intentionally designed the TSP "to minimize decision-making by the Government that might not allow private investment markets to maintain their stability and objectivity."⁵ The statutory restrictions on the FRTIB's investment-related discretion are unambiguous.

As explained more fully below, the restrictions reflect Congress's deliberate consideration of the potential trade-offs between protecting TSP participants' retirement savings from systemic market risks and protecting the market and TSP participants' retirement savings from the unique conflicts of interest inherent in the Federal government's management of the TSP.

Congress – not the FRTIB or the executive branch – dictates the TSP's investment menu.

FRTIB has less discretion than other retirement plan fiduciaries in setting investment policy. Most retirement plan fiduciaries have the discretionary authority to determine the number and type of investment funds that are available to their participants. The FRTIB, on the other hand, has no such authority. The number and types of investment options available to TSP participants are dictated by federal statute. Congress has provided an exhaustive list of the types of options the FRTIB can offer.⁶ The FRTIB cannot, without Congressional direction, expand or change this list. FERSA's legislative history evinces a clear intent to require Congressional approval to expand or change TSP investment options.⁷

³ See H.R. CONF. REP. 99-606, 1986 U.S.C.C.A.N. 1508, 1521 ("Unlike a defined benefit plan where an employer essentially promises a certain benefit, a thrift plan is an employee savings plan. In other words, the employees own the money. The money, in essence, is held in trust for the employee and managed and invested on the employee's behalf until the employee is eligible to receive it. This arrangement confers upon the employee property and other legal rights to the contributions and their earnings.").

⁴ *Id.*

⁵ S. REP. 99-166, S. 1986 U.S.C.C.A.N. 1405, 1457.

⁶ 5 U.S.C. § 8438(b)(1) ("The Board shall establish—(A) a Government Securities Investment Fund...(B) a Fixed Income Investment Fund...(C) a Common Stock Index Investment Fund...(D) a Small Capitalization Stock Index Investment Fund...(E) an International Stock Index Investment Fund ... and (F) a service that enables participants to invest in mutual funds, if the Board authorizes the mutual fund window...."); 5 U.S.C. 8438(c)(2) ("If an election has not been made with respect to any sums available for investment in the Thrift Savings Fund, the Executive Director shall invest such sums in an age-appropriate target date asset allocation investment fund....Such investment fund shall consist of any of the funds described in subsection (b).").

⁷ See H.R. CONF. REP. 99-606, 1986 U.S.C.C.A.N. 1508, 1519 ("The conferees chose to limit the number of funds....Should additional investment vehicles become desirable, the Congress can authorize them.").

The FRTIB is statutorily required to select indices that are “commonly recognized” and provide a “reasonably complete representation” of equity markets.

The FRTIB’s role in choosing TSP investments is limited to selecting indices for its Congressionally mandated index funds. But even in this small role, Congress has still further restricted the FRTIB’s discretion. When choosing indices for the TSP’s index funds, the FRTIB is limited to those that are “commonly recognized” and which are a “reasonably complete representation” of the entire market.

The FRTIB is prohibited from actively choosing or divesting the underlying securities in which TSP funds are invested.

FERSA says:

[T]he Board may not direct the Executive Director to invest or to cause to be invested any sums in the Thrift Savings Fund in a specific asset or to dispose of or cause to be disposed of any specific asset of such Fund. ⁸

Congress explained that this provision exists to address concerns that the executive branch’s power to invest assets of such extraordinary size could influence or disrupt markets.⁹ An early draft of FERSA included a provision that would have permitted the Executive Director to exclude stocks from the index funds upon the recommendation of the Employee Thrift Advisory Council, but that provision was not enacted by Congress.¹⁰ Instead, Congress enacted a provision for each TSP stock index fund, which says:

The portfolio shall be designed such that, to the extent practicable, the percentage of [the TSP fund] that is invested in each stock is the same as the percentage determined by dividing the aggregate market value of all shares of that stock by the aggregate market value of all shares of all stocks included in such index.¹¹

In other words, there are only two criteria that the FRTIB may use to determine how the underlying securities in the TSP index funds are to be invested: (1) the market value of stocks included in the index, and (2) factors that may make it impracticable to replicate the index exactly.

The FRTIB is prohibited from exercising shareholder voting rights associated with the underlying securities in which the TSP funds are invested.

⁸ 5 U.S.C. § 8472(g)(2).

⁹ See 131 Cong. Rec. 31065 (1985), available at <https://www.govinfo.gov/content/pkg/GPO-CRECB-1985-pt22/pdf/GPO-CRECB-1985-pt22-5-2.pdf> (“With a thrift fund of this size and scope for the Federal work force concern about the role of the Federal Government in operating this fund and its effect on the market is understandable. We have designed funds which are essentially self-managed and do not require extensive day-to-day investment decisions. Board members are prohibited by law from making specific investment decisions and from directing the Executive Director to make specific investment decisions.”).

¹⁰ *Id.* at 31055.

¹¹ 5 U.S.C. 8438(b)(2)(B), (3)(B), and (4)(B).

The FRTIB is categorically prohibited from using proxy voting power to influence corporate decisions. FERSA says:

The Board, other Government agencies, the Executive Director, an employee, a Member, a former employee, and a former Member may not exercise voting rights associated with the ownership of securities by the Thrift Savings Fund.¹²

This provision does not contain any exceptions for corporate decisions that may impact the value of the underlying securities in which the TSP funds are invested.

Conclusion

The FRTIB is well-aware of the discussion of climate-related financial risk in investment decision-making and portfolio construction. But the FRTIB's role in investment decision-making and portfolio construction is extraordinarily limited. Congress reserved investment discretion to itself to mitigate the risk that the FRTIB (or, by extension, the executive branch) might use the sheer size of the Thrift Savings Fund to manipulate the market in pursuit of national policy priorities.

I applaud the DOL's efforts to consider what steps can be taken to protect the retirement savings of U.S. workers and families from the threats of climate-related financial risk. As you do so, I urge you to bear in mind that neither the FRTIB nor any other Federal agency has the Constitutional authority to override the unambiguously expressed intent of Congress. A federal agency's power is constrained by the authority that Congress delegated it by statute.

The enclosed attachment contains my response to selected questions posed by the DOL's RFI. While the RFI covers a range of issues, I comment only on those matters where I believe the FRTIB's expertise is most relevant.

Thank you for your time and attention to these matters and for consideration of my comments. Please do not hesitate to contact me with any questions.

Sincerely,



Ravindra Deo
Executive Director

¹² 5 U.S.C. § 8438(f).

RESPONSE TO SELECTED QUESTIONS

QUESTION 8: 5 U.S.C. 8438 defines the specific types of investments that are permissible under the TSP. Given the scope of 5 U.S.C. 8438, what specific actions relating to FRTIB's consideration of ESG factors, including climate-related financial risks, when making investment decisions could and should EBSA take, consistent with EBSA's authority and role under FERSA, and why?

This question presupposes that the FRTIB makes investment decisions. This presupposition is undermined by the extent to which FERSA constrains the FRTIB's investment discretion. Congress – not the FRTIB or the executive branch – dictates the TSP's core investment menu. The FRTIB is statutorily required to select passive indices that are “commonly recognized” and provide a “reasonably complete representation” of the entire equity market. And the FRTIB is statutorily prohibited from actively choosing or divesting the underlying securities in which the TSP's index funds are invested.

QUESTION 9: The Executive Director and the members of the FRTIB are TSP fiduciaries, and are subject to the fiduciary responsibility and prohibited transaction provisions set forth at 5 U.S.C. 8477. FERSA requires the Department to, among other things, establish a program to carry out audits to determine the level of compliance with these standards and obligations. Those responsibilities have been delegated to EBSA, which implements a risk-based audit program that identifies risks and vulnerabilities, assesses the likelihood of harm from these risks and vulnerabilities, and considers the magnitude of potential damage associated with the various risks and vulnerabilities. FERSA also provides the Department with specific authority to prescribe regulations to carry out 5 U.S.C. 8477. How can EBSA best conduct an audit program, consistent with its authority and role under FERSA, that identifies and assesses the risks and vulnerabilities posed to TSP by climate change? What types of questions should the audit program answer? What data sources should EBSA use to answer them?

The DOL has the authority to conduct audits of the FRTIB and the TSP. Those audits have historically focused on ensuring that FRTIB complies with FERSA, sets policies and procedures that allow it to operate the TSP in compliance with FERSA and the FRTIB's regulations, and that the FRTIB follows those policies, procedures and regulations. We heartily support the DOL's audit program since it provides an independent perspective on the FRTIB's compliance with FERSA.

However, the DOL has never before audited the appropriateness of the TSP investment options, nor should it, since the investment options are dictated by Congress. Moreover, the DOL's interpretative authority over FERSA's statutory provisions is limited to sections 8477, 8478, and 8478a. The authority to interpret and implement the remainder of FERSA's provisions, including 5 U.S.C. 8438, belongs to the Executive Director of the

FRTIB.¹³ This question, therefore, implies that the DOL has a broader field of interpretative authority than is accurate.

QUESTION 10. A 2021 GAO Report recommended that FRTIB conduct a rigorous audit of TSP's exposure to climate-related financial risk. What data, if any, should FRTIB collect on TSP's exposure to climate-related financial risk? What types of data, if any, should it collect from asset managers regarding climate-related financial risk?

As explained in my letter, Congress requires the FRTIB to select stock index funds based on market capitalization and requires each fund to hold stocks in the same proportion as the stock's market weight. To the extent that the TSP index funds achieve the Congressional directive to hold essentially all stocks in proportion with their existence, the TSP cannot, by definition, over-invest or under-invest in any risk, including climate change. Congress intended for the FRTIB's stock index funds to be exactly as exposed to any risk, including climate-related financial risk, as the entire stock market. The TSP funds cannot have more climate-risk than the entire market, just as they cannot have any less climate-risk than the entire market. As such, an audit by the FRTIB of TSP's exposure to climate-related financial risk would not provide any actionable information.

Systemic market risks such as climate change require systemic solutions. Congress has created many federal agencies that, unlike the FRTIB, have the authority and expertise to address systemic market risks. Many of those federal agencies are members of the Financial Stability Oversight Council (FSOC), which is working urgently to understand and document the risks that climate change poses to the entire stock market.¹⁴ The FSOC's most recent report on climate-related financial risk identifies gaps in existing data as a critical impediment to assessing and addressing climate-related financial risk.

"While significant data related to climate change already exists, there remain gaps in connecting the science of climate change to financial risk assessments and real-world economic impacts."¹⁵

The FRTIB has no authority to impose itself into a domain of expertise that has been delegated by Congress to other federal agencies. But I assure you the FRTIB is not putting its head in the sand. The FRTIB is following the progress made by the Federal agencies who are members of the Financial Stability Oversight Council as they develop the data necessary to connect the science of climate change to financial risk assessments and real-world economic impacts. We will study their future reports and any future recommendations to determine whether and how they are applicable to the TSP so that we can make appropriate recommendations to Congress.

¹³ 5 U.S.C. 8474.

¹⁴ The FSOC was established by the Dodd Frank Wall Street Reform and Consumer Protection Act. One of the purposes of the Council under the Dodd-Frank Act is to respond to emerging threats to the stability of the U.S. financial system. The FSOC is composed of ten voting members who head the U.S. Department of the Treasury, the Board of Governors of the Federal Reserve System (Federal Reserve Board or FRB), the Office of the Comptroller of the Currency (OCC), the Consumer Financial Protection Bureau (Bureau or CFPB), the Securities and Exchange Commission (SEC), the Federal Deposit Insurance Corporation (FDIC), the Commodity Futures Trading Commission (CFTC), the Federal Housing Finance Agency (FHFA), and the National Credit Union Administration (NCUA).

¹⁵ Financial Stability Oversight Council, *Report on Climate-Related Financial Risk* (2021), available at <https://home.treasury.gov/system/files/261/FSOC-Climate-Report.pdf>, at page 23.

QUESTION 11. What information, if any, should the FRTIB collect on asset managers' policies, including their consideration of climate change and ESG factors in their stewardship and investment decision-making, and how their actual behavior corresponds to their stated policies? How could this data inform FRTIB's own decision-making and management of TSP?

As explained in my letter, the FRTIB has very little investment discretion. The FRTIB hires asset managers to implement a precise and predetermined Congressional mandate to mimic a specified index as closely as possible. The asset managers are contractually required to run the funds as Congress intended and prescribed and the asset managers assume fiduciary responsibility when they contract with the FRTIB.

FERSA expressly prohibits the FRTIB or other Federal agencies from exercising shareholder voting rights associated with the ownership of securities by the Thrift Savings Fund.¹⁶

The FRTIB contractually requires each TSP fund manager to have a proxy voting policy. But the FRTIB cannot—in accordance with FERSA's prohibition against the FRTIB exercising shareholder voting rights—dictate the contents of the fund managers' proxy voting policies. The FRTIB's role is limited to ensuring that the fund managers abide by their own proxy voting policies. Toward that end, each fund manager is contractually required to have an audit conducted of how they vote proxies and provide that audit to the FRTIB. The Chief Investment Officer shares that information with the Board members at their public monthly meeting. That report is then posted on frtib.gov.

QUESTION 12. What actions, if any, should the TSP's asset managers, take to incorporate climate-related financial risk, consistent with FERSA's terms and their duty of prudence?

See my response to QUESTION 11.

QUESTION 13. The TSP's fund offerings rely on passive index investing. Is there evidence that the indices relied upon by the TSP systematically underestimate or overestimate the risks associated with climate change, or that the market fails to appropriately factor in the risks associated with climate change in pricing publicly-traded assets?

See my response to QUESTION 10.

QUESTION 14. What analysis could FRTIB undertake to inform whether other possible indices may better take into account the risks posed by climate change? What analysis could FRTIB perform to weigh this feature against other characteristics of these indices such as their fees? What actions could FRTIB take to consider climate change and other material ESG factors in directing investment selection decisions for the TSP, consistent with FERSA's statutory requirement that indices be "commonly recognized" and a "reasonably complete representation" of the market?

¹⁶ 5 U.S.C. 8438(f).

While there are clearly ESG indices, to date none of them rise to the level of a “commonly recognized” index. The major index providers – FTSE, MSCI, S&P – all have developed non-customized indices that in one form or another incorporate unique versions of ESG investment strategies and index construction methodologies. The lack of standardization in the strategies and methodologies currently being used to construct ESG index funds precludes the ability to effectively compare one benchmark to another.

There is also a lack of standardization and reliability in corporate disclosures that inform the construction of ESG indices. The U.S. Securities Exchange Commission (SEC) has recently proposed regulatory efforts that may remedy this problem and facilitate the development of ESG indices that meet FERSA’s “commonly recognized” and “reasonably complete representation” requirements.¹⁷

The FRTIB is not ignoring changes in the market. We are closely monitoring recent innovations in index construction methodologies, as well as regulatory developments that may promote more reliable data about how ESG index providers create and apply their inclusion criteria.

QUESTION 15. Other than investments, are there any incentives that could be offered to encourage more effective incorporation of climate-related financial risks into TSP, using the regulatory authority delegated to the Secretary or other administrative authorities under FERSA?

As previously mentioned, the DOL’s statutory authority under FERSA is limited to sections 8477, 8478, and 8478a. The authority to interpret and implement the remainder of FERSA belongs to the Executive Director of the FRTIB. This question implies a greater degree of authority over the FRTIB than is appropriate or accurate.

QUESTION 16. Some material suggests that when plan participants know their plan offers ESG options, many will invest in them. See, e.g., ESG Options in 401(k) Plans Could Lead to Higher Contribution Rates According to Schroders Survey, (May 13, 2021), available at <https://www.schroders.com/en/us/private-investor/media-centre/retirement-survey-2021-esg/> (when plan participants know their plan offers ESG options, 90% invest in them). In a 2017 survey of TSP participants, twenty-two percent of respondents said they most want the TSP to offer a broader range of investment options. See Federal Retirement Thrift Investment Board: 2017 Participant Satisfaction Survey, P. 11, fig. 8 (2017) available at <https://www.frtib.gov/ReadingRoom/SurveysPart/TSP-Survey-Results-2017.pdf>. Are there additional data suggesting, measuring, or otherwise indicating whether federal employees’ prefer ESG-focused investments?

The FRTIB is aware that some of its participants want the ability to invest in other funds beyond the five core TSP funds. To address this, Congress authorized the FRTIB to offer a mutual fund window.¹⁸ The FRTIB will be

¹⁷ U.S. Securities Exchange Commission, Proposed Rule, *The Enhancement and Standardization of Climate-Related Disclosures for Investors*, 87 Fed. Reg. 21334 (published April 11, 2022), available at <https://www.federalregister.gov/documents/2022/04/11/2022-06342/the-enhancement-and-standardization-of-climate-related-disclosures-for-investors>.

¹⁸ See Thrift Savings Plan Enhancement Act of 2009, P.L. 111-31, Division B, Title I, § 104 (codified at 5 U.S.C. 8438(b)(5)(A)).

implementing a mutual fund window in the summer of 2022.¹⁹ The mutual fund window will allow TSP participants to take a portion of their TSP accounts “through the window” to invest in mutual funds, including mutual funds that are ESG-focused.

¹⁹ See *Mutual Fund Window*, 87 Fed. Reg. 27917 (May 10, 2022), available at <https://www.federalregister.gov/documents/2022/05/10/2022-09972/mutual-fund-window>.