December 13, 2021

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,

RMI's Center for Climate-Aligned Finance respectfully submits this letter in support of the Department's Proposed Rulemaking, *Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights* ("the Proposed Rulemaking").[1]

We applaud the Department for its thorough and carefully considered proposal. The Proposed Rulemaking would reverse the disruptive provisions in two rules adopted in late 2020, *Financial Factors in Selecting Plan Investments* and *Fiduciary Duties Regarding Proxy Voting and Shareholder Rights*. The effect of the 2020 rulemakings was the stifling of an ERISA fiduciary's otherwise prudent and appropriate consideration of environmental, social and governance ("ESG") factors in their investment decision-making and proxy voting. **The Proposed Rulemaking would fix this. However, the nature of climate-related risk and impacts, paired with fiduciaries' status quo bias, weak market signals, inadequate pricing of climate-related risks, and the urgency of addressing the climate crisis suggest regulatory guidance and coverage for US fiduciaries may need to be even more direct.**

Following an introduction to RMI and the Center, our comments first emphasize the importance of regulatory clarity for fiduciaries and then outline the Proposed Rulemaking's positive contributions. We then turn to a discussion on whether the Proposed Rulemaking provides sufficient coverage and clarity for fiduciaries to effectively address climate-related factors.

Background on RMI and our expertise

RMI is an independent nonprofit founded in 1982 that transforms global energy systems through market driven solutions to align with a 1.5°C future and secure a clean, prosperous, zero-carbon future for all. We work in the world's most critical geographies and engage businesses, policymakers, communities, and NGOs to identify and scale energy system interventions that will cut greenhouse gas emissions at least 50 percent by 2030.

In July 2020, RMI launched the Center for Climate-Aligned Finance ("the Center") to help the financial sector transition the global economy toward a zero-carbon, 1.5°C future.[2] Through deep partnerships in finance, industry, government, and civil society, the Center works to develop decarbonization agreements within high-emitting sectors and supports financial institutions to decarbonize their loan

[1] https://www.federalregister.gov/documents/2021/10/14/2021-22263/prudence-and-loyalty-in-selecting-plan-investments-and-exercising-shareholder-rights
[2] https://climatealignment.org/

books and investment portfolios. The Center also works to shape the financial sector's operating environment by addressing barriers common to all financial institutions, such as regulatory clarity.

RMI strongly believes a 1.5°C future is critical for mitigating systemic risks to US capital markets. The financial sector has a key role to play in enabling and accelerating this transition, and recent years have seen a rapid increase in "climate alignment'' commitments by the largest US financial institutions. Climate alignment is establishing a new paradigm for the financial sector with redefined expectations around the role for financial institutions in advancing the net-zero transition. However, without sufficient regulatory clarity, financial institutions often do not know how to move forward on integrating climate into financial decision-making to realize their climate goals and help mitigate climate-related financial risks, including systemic risks to the US financial sector.

Regulatory clarity is essential for fiduciaries

In recent years, financial institutions have themselves acknowledged the importance of climate change for financial performance, including through a growing number of pledges to align their lending and investing practices with global climate goals.[3] More than 450 financial firms have committed to the Glasgow Financial Alliance for Net Zero ("GFANZ") since its launch in April 2021, resulting in over $130 trillion committed to achieving net-zero emissions in the global economy.[4] Following COP26, over 40% of global banking assets (and growing) are now committed to achieving net zero by 2050.[5]

Despite increasing ambition, financial institutions face multiple barriers on the path to implementing their climate commitments.[6] Chief among these barriers, especially for US investors, is regulatory clarity. Without certainty that consideration of climate-related factors in financial decision-making is within their fiduciary mandate, financial institutions' hands are tied.

Globally, institutional investors integrate ESG in 72% of fund selections.[7] Yet, in the United States, less than 3% of 401(k) plans offer a single fund that considers ESG factors, translating into only 0.1% of total plan assets invested into ESG funds.[8] Unusually low levels of ESG investing amongst ERISA fiduciaries is difficult to reconcile with i) proof of financial returns, and ii) the reported priorities of US beneficiaries.

Mounting evidence suggests ESG- and climate-related investment strategies correlate with better returns, delivering higher upside and lower downside potential in both the short- and long-term. In the short term, one Blackrock study found that the vast majority of ESG and sustainability-focused indices outperformed their traditional market counterparts during market downturns in 2015, 2016, 2018, and in 2020.[9] In the long-run, Eccles et al. found that US companies with high-quality organizational management of ESG issues outperformed peers over an eighteen-year period.[10] In a meta study of over 190 academic papers focused on the financial performance of ESG and sustainable assets, 88% of researchers found that solid ESG practices resulted in better operational performance of firms.[11] Climate

[3] https://rmi.org/banks-and-climate-action-taking-stock-of-recent-commitments/
[4] https://www.gfanzero.com/press/amount-of-finance-committed-to-achieving-1-5c-now-at-scale-needed-to-deliver-the-transition/
[5] https://assets.bbhub.io/company/sites/63/2021/11/GFANZ-Progress-Report.pdf
[6] https://rmi.org/insight/navigating-five-barriers-to-climate-aligned-finance/
[7] https://www.im.natixis.com/us/resources/esg-investing-survey-2019
[8] https://www.psca.org/research/401k/63rdAR
[9] https://www.gbm.hsbc.com/insights/global-research/esg-stocks-did-best-in-corona-slump
[10] Robert G. Eccles, Ioannis Ioannou, George Serafeim (2014) The Impact of Corporate Sustainability on Organizational Processes and Performance. Management Science 60(11):2835-2857. https://doi.org/10.1287/mnsc.2014.1984
[11] https://arabesque.com/research/From_the_stockholder_to_the_stakeholder_web.pdf

risk management in particular has been linked to financial outperformance, with companies on CDP's Global Climate "A" List outperforming peer companies by 5.5% per annum.[12] These results are building consensus in the financial sector, with 60% of professional investors acknowledging alpha potential through ESG investing.[13]

Further, demand for ESG appears to outpace supply amongst ERISA plans. In a 2021 survey of US participants in defined contribution plans who were aware of ESG options, 90% opted to invest in those options.[14] Another survey revealed that 80% of Generation Z and 63% of Millennial respondents in the US and Canada have asked their financial adviser about sustainable investing.[15] These statistics beg the question of what is suppressing ESG consideration by US fiduciaries, and whether the US approach serves beneficiaries' best interests.

Our report, *Zeroing In: The US Financial Sector Perspective on Net-Zero Lending and Investing,*[16] is based on a series of workshops the Center held in December 2020 with US banks and institutional investors to understand challenges they face in implementing climate alignment commitments.[17] During these workshops, held shortly after the November 2020 rulemaking, regulatory uncertainty around fiduciary duty was cited as a key challenge for US investors looking to integrate climate objectives into decision-making.

The Proposed Rulemaking lessens uncertainty as to whether fiduciaries may consider ESG factors

The Proposed Rulemaking restores fiduciary authority to consider all relevant factors. Since 1978, Department regulations have required fiduciaries to consider all relevant factors when choosing among available investment options, proxy voting, and exercising shareholder rights. The *Financial Factors* rule replaced this well-understood legal standard with a new and ill-defined "pecuniary" test, causing considerable confusion. The Proposed Rulemaking appropriately eliminates this new term, restoring the traditional all-relevant-factors test.

The Proposed Rulemaking clarifies that investment options incorporating relevant climate and other ESG factors are eligible as defaults. We endorse the Department's rescission of the prohibition on certain investment alternatives being used as the Qualified Default Investment Alternative ("QDIA"). A fiduciary's responsibilities of prudence and loyalty are no different for a QDIA than for other plan investments, and if a participant does not wish to invest in the QDIA, they can select another investment vehicle. However, the ability to incorporate ESG and climate related factors in QDIAs enables fiduciaries to help reduce the systemic risk exposure of default retirement vehicles. Any other approach would, as the Department observes in the preamble, "only serve to harm participants by depriving them of otherwise financially prudent options as QDIAs."

The Proposed Rulemaking clarifies that ERISA plans may continue to make prudent investments that provide collateral benefits; however, the language may still be too narrow. The *Financial Factors* rule provided that non-financial factors that offer collateral benefits to beneficiaries could be used to decide between funds only where the funds are economically "indistinguishable" (a provision known as the

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[12] https://cdn.cdp.net/cdp-production/cms/reports/documents/000/005/234/original/CDP_NA_2019-20_Annual_Report.pdf?1591886351
[13] https://www.im.natixis.com/us/resources/esg-investing-survey-2019
[14] https://www.schroders.com/en/us/institutional/media-centre/retirement-survey-2021-esg/
[15] https://www.accenture.com/_acnmedia/PDF-162/Accenture-Wealth-Management-Consumer-Report-New-State-of-Advice.pdf#zoom=40
[16] https://rmi.org/insight/zeroing-in/
[17] Ibid.

"tie-breaker rule"). This untenable standard effectively prohibited the use of collateral benefits altogether, a stark departure from longstanding Department guidance. While the Proposed Rulemaking's "equally serve the financial interests of the plan" language is an improvement on the term "indistinguishable," we suggest that the language is still too narrow. The issue is not how closely two or more investments resemble one another, but whether they are each the product of a prudent selection process. Fiduciaries should receive equal deference if their investment choice is the product of such a process. We believe it is more appropriate for the collateral benefit provision in the final rule to focus on whether investments are equally prudent (i.e., the output of a prudent fiduciary process), rather than on an analysis of the equivalence of their financial characteristics.

The Proposed Rulemaking restores fiduciary authority to make prudent decisions in proxy voting. We strongly support the ability of ERISA plan fiduciaries to exercise their judgment to vote proxies in the best interest of participants and beneficiaries. ERISA's fiduciary duties include active ownership, including informed proxy voting on shareholder proposals affecting companies owned by the plan. Fiduciaries must be given discretion to vote on these proposals, exercising critical oversight that has been shown to reduce downside risk.[18] We support the Proposed Rulemaking's revisions to the current rule, rightfully restoring a fiduciary's ability to vote on a wide array of important issues, including climate change.

Exercising shareholder rights is one of the most important levers financial institutions have to influence the real economy.[19] At the Center for Climate-Aligned Finance, we believe "a vote in favor of a proposal can provide a powerful signal for change".[20] In recent years, shareholder action on climate change has been growing,[21] and we expect to see more climate-oriented resolutions with the Securities and Exchange Commission's November 2021 guidance that shareholder proposals can "raise issues of broad social or ethical concern related to the company's business".[22] It is critical that fiduciaries feel empowered to exercise voting rights on these increasingly prevalent shareholder considerations.

Based on a review of empirical studies, Kölbel et al. find that "shareholder engagement emerges as the most reliable mechanism for investors seeking impact".[23] Despite "strong evidence that shareholder engagement is an effective mechanism through which investors can trigger reforms that improve the quality of company activities", the report also cites that, even of investments taking ESG factors into account, shareholder engagement is only practiced for 10% of assets in the United States.[24] Together, these findings suggest shareholder engagement is a reliable yet underutilized mechanism for fiduciaries to improve value for beneficiaries.

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[18] Hoepner, Andreas G. F. and Oikonomou, Ioannis and Sautner, Zacharias and Starks, Laura T. and Zhou, Xiaoyan, ESG Shareholder Engagement and Downside Risk (April 30, 2021). AFA 2018 paper, European Corporate Governance Institute – Finance Working Paper No. 671/2020, Available at SSRN: https://ssrn.com/abstract=2874252 or http://dx.doi.org/10.2139/ssrn.2874252

[19] https://rmi.org/insight/breaking-the-code/

[20] https://rmi.org/financing-1-5c-climate-resolutions-gather-momentum/

[21] https://rmi.org/shareholders-keep-up-the-pressure-on-corporate-climate-action/

[22] https://www.sec.gov/corpfin/staff-legal-bulletin-14l-shareholder-proposals

[23] Kölbel, Julian and Heeb, Florian and Paetzold, Falko and Busch, Timo, Can Sustainable Investing Save the World? Reviewing the Mechanisms of Investor Impact (July 20, 2019). Kölbel, Julian F., Florian Heeb, Falko Paetzold, and Timo Busch. in press. 'Can Sustainable Investing Save the World? Reviewing the Mechanisms of Investor Impact'. Organization & Environment. Available at: https://doi.org/10.1177/1086026620919202 , Available at SSRN: https://ssrn.com/abstract=3289544 or http://dx.doi.org/10.2139/ssrn.3289544

[24] Ibid.

While the Proposed Rulemaking would add much needed clarity, even stronger guidance may be warranted for climate factors

At the Center for Climate-Aligned Finance, our focus is on climate-related factors specifically, which we believe to be a relevant risk-return consideration for all investment and proxy voting decisions.[25] We support the Department upholding longstanding guidance by providing clarity that "a fiduciary may consider *any* factor material to the risk-return analysis, including climate change and other ESG factors".[26] We also appreciate the acknowledgement that "ESG considerations, including climate-related financial risk are, in appropriate cases, risk-return factors that fiduciaries should take into account when selecting and monitoring plan investments and investment courses of action." However, for the following reasons, we are concerned the proposed guidance may not yet provide adequate motivation and coverage for fiduciaries to consider climate-related factors in today's markets.

As a separate but related point, we echo a comment by Ceres in their comments to this Proposed Rulemaking on the Department's use of the word "material" in subparagraph (b)(4):

> For more than 40 years, since the Department adopted the original investment duties regulation in 1979, the standard for ERISA fiduciary duty has been to take into account all "relevant" factors. […] The word "material" was never part of the ERISA fiduciary analysis until it was inserted in the 2020 Rule. There is a huge body of decisional and regulatory law underpinning the word "material" in the context of the federal securities laws, and the subparagraph might be read as importing that law. There is no reason to introduce a new term, inviting new interpretations of well-settled fiduciary concepts in ERISA. The word "relevant" in this context is preferable to "material."[27]

Climate change represents a systemic risk with economy-wide implications, challenging traditional approaches to risk-return analysis

The magnitude, timing, and location of climate-related financial risks may be subject to uncertainty, but the systemic nature of climate-related risks – characterized by widespread and interlinked exposures – means their impacts can quickly compound, impacting markets and financial performance economy-wide.

As the Financial Stability Oversight Council ("FSOC") acknowledges, climate change represents a *systemic risk* to financial stability.[28] Beyond climate-related financial risks to individual assets, systemic risks are undiversifiable and interconnected across the financial sector as a whole. As a result, climate change impacts may result from dynamic and disperse exposures, including through amplified feedback loops across global economies. We elaborate on the implications in a recent blog assessing FSOC's Report on Climate-Related Financial Risk ("the FSOC Report"):

[25] Our comments are not intended to suggest fiduciaries should consider climate at the expense of or more than other ESG factors, but since our work focuses on climate specifically, our comments focus on the "presumptive materiality" of climate-related factors.

[26] https://public-inspection.federalregister.gov/2021-22263.pdf

[27] https://www.ceres.org/sites/default/files/Ceres%20letter%20DOL%202021.pdf

[28] https://home.treasury.gov/system/files/261/FSOC-Climate-Report.pdf

Center for Climate Aligned Finance

> Systemic risk means that one financial actor's vulnerability (or climate risk exposure) can jeopardize the well-being of other financial actors, corporates, and households economy-wide. Like dominoes, systemic risks can be passed through "transmission channels," impacting seemingly disconnected parts of the economy. Acknowledging that climate risks are dynamic and interconnected directly challenges traditional approaches to assessing materiality and risk on an individual asset basis. Instead, systemic risks such as these must be assessed across an entire portfolio or the financial system as a whole.[29]

While physical risks refer to the costs from acute, climate-related disaster events, they can lead to collateral damage by disrupting global resource availability and accessibility, supply chains, and labor forces. Climate related disasters are increasingly frequent, with a record 22 events in the US during 2020 alone, each of which has been assessed to result in over $1 billion in damage for a total cost of $100 billion.[30] However, the systemic nature of climate-related risks and transmission pathways suggests total damages could be much higher.

Across real economy sectors, decarbonization to mitigate the worst impacts of climate change will require a structural overhaul of core business models and production methods. This transition will be costly and challenging to many individual firms, especially smaller companies. However, as the FSOC Report acknowledges, the transition is also inevitable and already under way. Widespread market changes are evidenced by breakthrough, low-carbon technologies undercutting incumbent alternatives across markets and increasingly triggering their early retirement.[31] Market shifts can also be observed through mounting legal liabilities for companies that uphold the status quo, especially as international regulatory and policy regimes embrace updated policies, tools, and guidance.[32] The direction of travel is unmistakable, and unprepared actors face significantly higher risk exposures and also augment systemic risks by impeding a smooth and orderly transition.

COVID-19 provides a case study in how systemic risks can be difficult to capture. Following global travel bans due to COVID-19, the risk implications for an index of aviation stocks was likely clear. However, the transmission of COVID-induced risks to semiconductor markets was likely more difficult to predict. For instance, consider the interplay between risks transmitted from economic slowdown leading to layoffs, to slowed production, to delayed shipping with the compounding factors of increased consumer demand for durable goods and unprecedented recovery spending by international governments, among others.[33] Climate change risks are analogous. While the direct, physical risks that climate poses to, for instance, investments in coastal properties may be clear, the transmission pathways for climate-related risk factors across entire investment portfolios may not be.

Because of the systemic nature of climate-related financial risks, we believe climate is a relevant factor for fiduciaries seeking to protect beneficiaries' best interests. As universal owners,[34] ERISA fiduciaries

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[29] https://rmi.org/we-read-a-130-page-report-on-climate-regulation-so-you-dont-have-to/
[30] https://www.ncdc.noaa.gov/billions/events
[31] https://rmi.org/how-to-retire-early-making-accelerated-coal-phaseout-feasible-and-just/
[32] https://www.unepfi.org/wordpress/wp-content/uploads/2019/10/Fiduciary-duty-21st-century-final-report.pdf
[33] https://www.nytimes.com/interactive/2021/12/05/business/economy/supply-chain.html
[34] Quigley, Ellen, Universal Ownership in Practice: A Practical Investment Framework for Asset Owners (May 28, 2020). Winner of Best Paper for Potential Impact on Sustainable Finance Practices, GRASFI 2020, Available at SSRN: https://ssrn.com/abstract=3638217 or http://dx.doi.org/10.2139/ssrn.3638217

face asset-level exposures to physical and transition financial risks, in addition to systemic climate risk, across real economy sectors. Proactive risk mitigation measures can help mitigate negative impacts. If fiduciaries interpret prevailing guidance to invite additional scrutiny for consideration of climate change-related factors, especially if assets ultimately underperform, consideration of climate may remain overly stymied relative to other factors. Fiduciaries can only take steps to proactively manage and mitigate systemic climate risks if they have the regulatory greenlight to do so.

Status quo bias may lead to inefficient integration of climate by fiduciaries, even where it is financially relevant to risk-return

As the FSOC Report acknowledges, significant challenges remain in linking and assessing the complex transmission pathways between climate change's physical and transition risks to the financial sector and global economy. Accordingly, many aspects of climate risk, especially those that may not be imminent or directly linked to investments, may elude the boundaries of conventional materiality or risk-return evaluations. Misperception of risk-return is reinforced by conventional investing and lending approaches that may not be suited to capture climate-related risk-return factors.

In its report *Managing Climate Risk in the U.S. Financial System*, the Commodity Futures Trading Commission ("CFTC") describes how conventional approaches to capital allocation may fall short in capturing the full scope of climate risk-return implications:

> Asset owners and managers set investment strategies and evaluate returns based on benchmarks and strategic asset-allocation targets. Managed funds often raise capital based on explicit terms including investment theses and lock-up periods ranging from months to years. Return targets tend to be based on historical returns or on capital market forecasts premised on economic growth and other factors. This practice drives a strong status quo bias that undermines a more complete evaluation of what the future may bring, including future opportunities associated with managing climate risk. Without a historical track record or clear empirical justification, it is often difficult for traditional investors to integrate sustainable investments into their portfolios.[35]

The Center's recent report, *Zeroing In: The US Financial Sector Perspective on Net-Zero Lending and Investing*, is based on a series of workshops RMI held in December 2020 with US banks and institutional investors to understand challenges they face in implementing climate alignment commitments. During these workshops, institutional investors described how engrained interpretations of fiduciary duty encumber institutional change, even as market demands and operating environments evolve. The report explains:

> For institutional investors, overcoming cultural challenges would be supported indirectly by a clarification of the regulatory uncertainty for fiduciaries in the United States. The lack of regulatory clarity on fiduciary duty, specifically as it relates to ESG, has led to a solidification of organizational cultures that prioritize a constrained definition of the actions that an

[35] Climate-Related Market Risk Subcommittee (2020). Managing Climate Risk in the U.S. Financial System. Washington, D.C.: U.S. Commodity Futures Trading Commission, Market Risk Advisory Committee.

institutional investor can take to place climate at the core of investment strategies. Some institutional investor participants pointed to the specific barriers to gaining consensus on an investment strategy that prioritizes climate from portfolio managers, whose sole responsibility is to uphold their fiduciary duty when making investment decisions on behalf of clients. [36]

This issue is compounded by the mispricing of climate risk in financial assets, with 93% of institutional investors in agreement that climate change as an investment risk has yet to be priced into key markets globally.[37] While estimates vary, the global economy potentially faces at least $11.8 trillion of assets at risk of being stranded by climate change and subsequent business and policy shifts.[38] For instance, nearly 60% of oil and gas and 90% of coal reserves must remain unextracted to stay within the limits of global climate goals.[39]

Paragraph (c)(3) of the Proposed Rulemaking states that if "a fiduciary prudently concludes that competing investments, or competing investment courses of action, equally serve the financial interests of the plan over the appropriate time horizon, the fiduciary is not prohibited from selecting the investment, or investment course of action, based on collateral benefits other than investment returns"[40]. However, both status quo bias and inadequate pricing of climate risk in the market impact may thwart accurate risk-return assessments, impeding efficient capital allocation by ERISA fiduciaries.

The case for stronger regulatory guidance on climate

The unprecedented and universal nature of climate-related risks, as well as the dire urgency of addressing those risks, calls for consideration of novel regulatory guidance and approaches. As the FSOC Report notes, "financial risks associated with climate transitions likely increase if such transitions are delayed and occur in an unanticipated, abrupt manner."[41]

Amongst US financial regulators, a principles-based approach to clarifying the relevance of climate-related financial risks has largely fallen short of its intent. The Secretaries and Exchange Commission ("SEC")'s 2010 Climate Change Guidance "noted that, depending on the circumstances, information about climate change-related risks and opportunities might be required in a registrant's disclosures related to its description of business, legal proceedings, risk factors, and management's discussion and analysis of financial condition and results of operations."[42] Yet, in 2021, the SEC identified a need to revisit this guidance due to lagging climate-related disclosure practices by public issuers relative to evolving investor demands with respect to climate change. US investor surveys report growing dissatisfaction with the current state of ESG risk disclosures by public companies.[43] As SEC Chair Gary Gensler has explained:

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[36] https://rmi.org/insight/zeroing-in/

[37] https://investmentsandwealth.org/getmedia/73598b76-2523-4d0d-a0ae-3aad8586d237/future-2024-abridged-us-final.pdf

[38] IRENA (2020), Global Renewables Outlook: Energy transformation 2050 (Edition: 2020), International Renewable Energy Agency, Abu Dhabi. ISBN 978-92-9260-238-3

[39] Welsby, D., Price, J., Pye, S. et al. Unextractable fossil fuels in a 1.5 °C world. Nature 597, 230–234 (2021). https://doi.org/10.1038/s41586-021-03821-8

[40] https://www.sec.gov/comments/climate-disclosure/cll12-8931891-245387.pdf

[41] https://home.treasury.gov/system/files/261/FSOC-Climate-Report.pdf

[42] https://www.sec.gov/news/public-statement/lee-climate-change-disclosures

[43] https://www.ey.com/en_us/assurance/how-will-esg-performance-shape-your-future

In 2010, the SEC offered guidance on climate risk disclosure. A lot has changed since then, though, and investors don't have the ability to compare company disclosures to the degree that they need. For example, a review of S&P 500 issuers' filings after the SEC's 2010 guidance found filers generally did not engage in "quantifying risks or past impacts" with respect to climate. They also tended to use "boilerplate language of minimal utility to investors.[44]

Further, the Proposed Rulemaking states that "for many years, the Department's non-regulatory guidance has recognized that, under the appropriate circumstances, ERISA fiduciaries can make investment decisions that reflect climate change and other environmental, social, or governance ("ESG") considerations, including climate-related financial risk […]"[45]. Nonetheless, US retirement plans offered a dearth of ESG options for retirement plans since before the November 2020 rulemaking.[46]

Finally, the importance of regulatory clarity is reinforced in a litigious market. In an international comparison of fiduciary duty across jurisdictions, a 2020 report by the law firm Freshfields Bruckhaus Deringer LLP highlights the implications of a highly litigious environment for US fiduciaries:

> Asset Owners and their Investment Advisers will need to determine prior to taking any action whether or not a litigator could successfully posit a causal link between such activities and any adverse impact on financial return and thereby prove a breach of their duties as a result of pursuing such activities.[47]

Internationally, a paradigm shift among regulators and policymakers has clarified that ESG incorporation and active management of associated financial risks are core to fiduciary duty. Globally, over 730 policy revisions across over 500 policy instruments support, encourage, or require investors to consider long-term investment factors like ESG issues.[48] Strengthened, explicit guidance to ERISA fiduciaries that climate has financial implications to the risk and investment return of assets across the global economy would greatly help to reduce any lingering uncertainty as to whether and when climate-related factors *should* be considered in risk-return assessments.

Domestically, the Department should strive to provide fiduciaries guidance on the significance of climate change for risk-return evaluations that, at minimum, match the baseline ambition of peer regulators. The Securities and Exchange Commission[49], the Office of the Comptroller of the Currency[50], and the Commodity Futures Trading Commission[51] have all made statements or taken steps to treat climate-related financial factors as relevant to financial actors, marking a reevaluation of previous guidance in light of challenges and novel circumstances presented by climate change. Further, the treatment of

[44] https://www.sec.gov/news/speech/gensler-pri-2021-07-28
[45] https://public-inspection.federalregister.gov/2021-22263.pdf
[46] https://www.ussif.org/files/Publications/SIF_2017PlanSponsors_F.pdf
[47] https://www.freshfields.us/4a199a/globalassets/our-thinking/campaigns/legal-framework-for-impact/a-legal-framework-for-impact.pdf
[48] https://www.unepfi.org/wordpress/wp-content/uploads/2019/10/Fiduciary-duty-21st-century-final-report.pdf
[49] https://www.sec.gov/news/speech/lee-playing-long-game-110520; "OCC" see https://www.ots.treas.gov/news-issuances/speeches/2021/pub-speech-2021-116.pdf
[50] https://www.ots.treas.gov/news-issuances/speeches/2021/pub-speech-2021-116.pdf
[51] Climate-Related Market Risk Subcommittee (2020). Managing Climate Risk in the U.S. Financial System. Washington, D.C.: U.S. Commodity Futures Trading Commission, Market Risk Advisory Committee.

climate risks as a considerable systemic risk for all assets would be in line with recommendations issued by FSOC and the White House.

Conclusion

We are pleased by the Department's actions on this urgent issue, and we hope to see continued attention from the Department to ensure regulatory clarity for ERISA fiduciaries around consideration of ESG and climate-related factors in selecting investments and exercising shareholder rights.

To summarize our priority messages:

- Regulatory certainty around fiduciary duty is crucial for ERISA fiduciaries, especially as an increasing number of financial institutions look to implement various climate commitments and plan participant demand for ESG options increases.
- We applaud the Proposed Rulemaking for clarifying fiduciary duty with respect to consideration of ESG and climate-related factors.
- While the Proposed Rulemaking includes welcome provisions toward clarifying the legality of a fiduciary's consideration of climate and ESG factors, we are concerned that it may not yet provide sufficient cover or a strong enough signal to facilitate appropriate integration of climate by US fiduciaries.
    - For one, climate change is a systemic risk with economy-wide implications that may not be easily captured by traditional approaches to assessing materiality or risk-return factors.
    - Additionally, status quo bias and path dependency among financial institutions, as well as ongoing mispricing of climate risks by the market, risk concealing the relevance of climate for risk-return assessments, further slowing appropriate and efficient consideration of climate.
    - Finally, financial regulatory guidance on ESG and climate change is evolving (globally and domestically), and ERISA fiduciaries may seek exceptionally clear guidance given litigious precedent.

Thank you very much for your consideration of our comments herein. If there are questions on the points highlighted here, or if you would like further information, please reach out to Whitney Mann at WMann@rmi.org and Alex Murray at AMurray@rmi.org.

Sincerely,

Brian O'Hanlon

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