Modernizing Fiduciary Duty Fact Sheet

Problem

- Enhanced disclosures regarding Environmental, Social, and Governance (ESG) factors will likely be ineffective in materially changing corporate behavior unless the beneficiaries of these disclosures – investors and the public – have established processes to review, analyze, and act upon them.
- The federal securities laws, ERISA, the commodities laws, and relevant state laws generally do not explicitly mandate investment fiduciaries to take any action to consider ESG-related issues.
- In some cases, investment fiduciaries may be precluded from considering ESG factors when making investment decisions, and the Dep't of Labor has proposed even preventing ERISA Plan fiduciaries from voting on some shareholder proposals.
- Retirees and other investors want to know how their funds and plans are considering ESG-related risks and opportunities, but there's no standard, reliable, comparable disclosures by their fiduciaries.
- Given strong investor interest in ESG-related products (and often higher fees for those products), there is a growing risk of "greenwashing" by investment fiduciaries. Rigorous standards are necessary to enure that disclosures are honest and meaningful.

Solution

- Securities and Exchange Commission should adopt rules under the Investment Advisers Act of 1940 to require investment advisers to have policies and procedures to identify and assess relevant ESG factors.
    - Policies and procedures should be audited and publicly disclosed.
- Dep't of Labor should revise its October 30, 2020 rule on Financial Factors in Selecting Plan Investments to permit Qualified Default Investment Alternatives (QDIAs) to include funds that consider ESG factors.
- Dep't of Labor should require ERISA Plan fiduciaries to adopt policies and procedures to identify and assess relevant ESG factors.
    - Policies and procedures should be audited and publicly disclosed.
- Factors to be considered should include, but not be limited to: physical and transition climate risks, worker and executive diversity, worker wages, and political spending.
    - NOTE: These proposals do not impact the duties of care or loyalty, or override the judgment of fiduciaries, but instead require formal processes for identification and consideration of ESG factors.

Opportunity for the US to Go from Laggard to Leader

- Investment managers around the globe already view considering ESG factors as essential to fulfilling their fiduciary duties (see, e.g., UN PRI 21st Century Report).

- Other global markets (e.g., Canada, EU, and the United Kingdom) have been incorporating ESG issues into investment fiduciaries' duties.
    - Example: The 2016 Canada Pension Benefits Act requires pension plans to disclose "whether ESG factors are incorporated into the plan's investment policies" and, if so, how.
    - Example: In August 2020, the United Kingdom proposed requiring defined benefit and defined contribution schemes to have detailed, public policies for identifying, assessing, and addressing ESG issues.
- In part, due to the size of asset management, any new US standard for Sustainable Investment Policies would likely quickly become the global standard for (1) factors to consider, (2) methods for consideration, (3) documentation and audit requirements, and (4) comparability.

Climate Impact

- Billions of dollars in funds that consider ESG factors that are currently QDIAs would be able to stay (as opposed to being taken out).
- Because many non-ESG-branded products and funds want access to the ERISA marketplace, many funds in the US do not currently consider ESG factors. This would eliminate that barrier, which would free up many non-"ESG"-branded funds and products to begin consideration of ESG factors.

Relevant Documents

- UNEP Finance Initiative and UN Principle for Responsible Investment, Fiduciary Duty in the 21st Century, Final Report, 2019, *available at* https://www.unpri.org/download?ac=9792
- Center for American Progress, Modernizing the Social Contract With Investment Fiduciaries, Nov. 2020, *available at* https://www.americanprogress.org/issues/economy/reports/2020/11/18/492982/modernizing-social-contract-investment-fiduciaries/.
- Press Release, Rep. Andy Levin (D-MI), Nov. 2020, *available at* https://andylevin.house.gov/media/press-releases/levin-statement-department-labor-rule-targeting-sustainable-investments.
- U.K. Department of Work and Pensions, Taking action on climate risk: improving governance and reporting by occupational pension schemes, 2020, *available at* https://www.gov.uk/government/consultations/taking-action-on-climate-risk-improving-governance-and-reporting-by-occupational-pension-schemes.
- Dep't of Labor, Fact Sheet: Final Rule on Financial Factors in Selecting Plan Investments, Oct. 2020, *available at*

https://www.dol.gov/sites/dolgov/files/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/final-rule-on-financial-factors-in-selecting-plan-investments.pdf.

- Dep't of Labor, Fact Sheet: Notice of Proposed Rulemaking on Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, Aug. 2020, available at https://www.dol.gov/sites/dolgov/files/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/fiduciary-duties-regarding-proxy-voting-and-shareholder-rights.pdf.