



## DOL Proposed Rulemaking on ESGs

On June 23, 2020, the U.S. Department of Labor (DOL) announced a proposed rule intended to provide clear regulatory guideposts for plan fiduciaries in light of recent trends involving environmental, social and governance (ESG) investing.

ESG criteria are a group of standards used by socially conscious investors to screen investments—and basically, the DOL strongly cautions against them when it comes to Employee Retirement Income Security Act (ERISA) plan fiduciaries.

As a plan fiduciary, one's primary obligation is to do what is in the best interests of the plan's participants. The DOL's proposed rule maintains that ESG vehicles, which can sacrifice investment returns or take on additional risk in the name of social responsibility, are not suitable as a qualified default investment.

## The proposal would make five core additions to the regulation:

- New regulatory text to codify the Department's longstanding position that ERISA requires plan fiduciaries to select investments and investment courses of action based on financial considerations relevant to the risk-adjusted economic value of a particular investment or investment course of action.
- An express regulatory provision stating that compliance with the exclusive-purpose (i.e., loyalty) duty in ERISA section 404(a)(1)(A) prohibits fiduciaries from subordinating the interests of plan participants and beneficiaries in retirement income and financial benefits under the plan to non-pecuniary goals.
- A new provision that requires fiduciaries to consider other available investments to meet their prudence and loyalty duties under ERISA.
- The proposal acknowledges that ESG factors can be pecuniary factors, but only if they present economic risks or opportunities that qualified investment professionals would treat as material economic considerations under generally accepted investment theories. The proposal adds new regulatory text on required investment analysis and documentation requirements in the rare circumstances when fiduciaries are choosing among truly economically "indistinguishable" investments.
- A new provision on selecting designated investment alternatives for 401(k)-type plans. The proposal reiterates the Department's view that the prudence and loyalty standards set forth in ERISA apply to a fiduciary's selection of an investment alternative to be offered to plan participants and beneficiaries in an individual account plan (commonly referred to as a 401(k)-type plan). The proposal describes the requirements for selecting investment alternatives for such plans that purport to pursue one or more environmental, social, and corporate governance-oriented objectives in their investment mandates or that include such parameters in the fund name.

At this point this is only a proposed – not an established – rule and remains an issue that we will continue to monitor and provide updates.

Contact the Pentegra Solutions Center at [solutions@pentegra.com](mailto:solutions@pentegra.com) or 855-549-6689 for expert guidance on how to make the most of the new rules.

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