



## ALERTS

### Department Of Labor Issues Proposed Rule On ESG Investing

October 2, 2020

#### Highlights

The DOL's Proposed Rule makes ESG investing more challenging for plan fiduciaries.

Fiduciaries may only consider pecuniary factors in selecting investments and investment courses of action.

ESG factors may be considered if they constitute material economic considerations. An ESG fund may not be a qualified default investment alternative.

Retirement plan participants and fiduciaries continue to express heightened interest in investing in environmental, social and governance (ESG) funds. ESG funds are generally funds featuring one or more environmental, social, governance, or similarly oriented assessments or judgments in their investment mandates. Plan fiduciaries responsible for investment decisions often explore ways to select ESG funds while still satisfying their fiduciary duties under ERISA.

ERISA requires that plan fiduciaries act "solely" in the interest of plan participants and beneficiaries and for the "exclusive purpose" of providing benefits and paying reasonable administrative expenses. A plan fiduciary

## RELATED PEOPLE



**Lori L. Shannon**

Partner  
Chicago

P 312-214-5664  
F 312-759-5646  
[lori.shannon@btlaw.com](mailto:lori.shannon@btlaw.com)

## RELATED PRACTICE AREAS

Benefits and Compensation  
Corporate  
Environmental, Social and Governance

must satisfy the duties of prudence and loyalty in selecting investments and investment courses of action for a plan.

Growing concern by the DOL over the consideration of non-economic factors in the selection of ESG funds as plan investments prompted the DOL to issue the Financial Factors in Selecting Plan Investments [Proposed Rule](#), which modifies prior guidance and makes it somewhat more challenging for plan fiduciaries to select ESG funds.

Prior guidance from the Department of Labor (DOL) regarding ESG investing permits a plan fiduciary to select an ESG fund over another investment fund under the “all things being equal” test, which allows consideration of non-economic factors as a tie-breaker for two equivalent investments.

The proposed rule provides the following clarifications:

- As a general rule, investments and investment courses of action must be selected based on pecuniary factors and not on the basis of any non-pecuniary factor in order for a fiduciary to satisfy their duties of prudence and loyalty. The “bottom line” of participants and beneficiaries must be the key factor in investment fund selection, and the interest of participants and beneficiaries must be superior to any other interest.
- Fiduciaries must compare investments or investment courses of action, solely based on economic factors, such as diversification, liquidity and rate of return. Plan fiduciaries are obligated to focus on obtaining the best economic result for the plan and should not be distracted by non-pecuniary factors in comparing investment alternatives.
- ESG factors may be considered if they “present economic risks or opportunities that qualified investment professionals would treat as material economic considerations under generally accepted investment theories.”
- In the rare case that a “tiebreaker” is necessary for economically equivalent investments, ESG factors may be considered if the fiduciary documents why the investments are considered equal, as well as why the ESG fund was chosen. This requirement is intended to retain but modify the “all things being equal” test, while preventing fiduciaries from making decisions based on non-pecuniary factors without proper consideration.
- Special rules apply to ensure ERISA compliance when ESG funds are included as investment alternatives under a defined contribution plan:
  - The fiduciary must use objective risk-return criteria to select and monitor all investment alternatives in the plan, including any ESG fund offered as an investment alternative;
  - The fiduciary must document its selection and monitoring of the investment; and

- o The ESG fund may not be the plan's qualified default investment alternative.

The DOL received many comments on the Proposed Rule from interested stakeholders through the comment period, which ended on July 30, 2020. Some practitioners anticipate that the Proposed Rule will be finalized in 2020, with the effective date occurring 60 days after it is published in the Federal Register. Though, it is possible that the final rule will ultimately be less restrictive than the Proposed Rule if the DOL considers comments of stakeholders who believe the Proposed Rule goes too far to prevent the availability of ESG investing.

To obtain more information, please contact the Barnes & Thornburg attorney with whom you work or Lori Shannon at 312-214-5664 or [lori.shannon@btlaw.com](mailto:lori.shannon@btlaw.com).

*© 2020 Barnes & Thornburg LLP. All Rights Reserved. This page, and all information on it, is proprietary and the property of Barnes & Thornburg LLP. It may not be reproduced, in any form, without the express written consent of Barnes & Thornburg LLP.*

*This Barnes & Thornburg LLP publication should not be construed as legal advice or legal opinion on any specific facts or circumstances. The contents are intended for general informational purposes only, and you are urged to consult your own lawyer on any specific legal questions you may have concerning your situation.*