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Are 401(k) plans in danger of not being green enough?

A recent retirement plan lawsuit raises the question of whether climate change exposes them to legal risk

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By **Greg Iacurci**

As the broad world of investors has embraced a more climate-friendly lens, 401(k) plans have lagged behind. But are 401(k) plan sponsors exposing themselves to legal trouble as a result?

A 24-year-old Australian environmental scientist **sued his A$57 billion ($39 billion) retirement fund** in federal court for not adequately disclosing or assessing the impact of climate change on its investments.

The plaintiff, Mark McVeigh, claims the Retail Employees Superannuation Trust, a type of defined-contribution arrangement, breached its fiduciary duty by failing to protect his savings against the adverse financial effects of rising world temperatures.

Would this be a winning argument in the U.S.? Legal experts aren't convinced.

"I don't think there's a cause of action under ERISA for being 'woke,'" Marcia Wagner, principal of The Wagner Law Group, said, referring to the Employee Retirement Income Security Act of 1974 and being environmentally conscious.

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In recent years, 401(k) plan participants have brought an increasing number of lawsuits against employers for breaching their fiduciary duties under ERISA. Those lawsuits typically hinge on the employer acting imprudently, for example by allowing excessive fees to be charged for plan investments.

In the case of a theoretical environmental claim, a plaintiff would have to prove that the 401(k) plan sponsor acted imprudently by not taking

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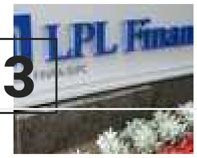
3 

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climate change or green issues into account, and that in turn negatively affected plan participants, according to attorneys familiar with retirement law.

"That to me is a very high bar," said Andrew Oringer, co-chair of the employee benefits and executive compensation group at Dechert, a law firm.

"There are plenty of people who try to make the case you can take green issues into account without being imprudent," Mr. Oringer said. "But to flip that and say you must take green issues into account, I don't think we've come that far yet."

In the U.S., investors have put $12 trillion into sustainable investments, which use environmental, social and governance criteria to guide investment decisions. That's about 26% of the $47 trillion of professionally managed assets in the U.S. at the end of 2017, according to the Forum for Sustainable and Responsible Investment.

Enthusiasm for such an investment style appears to be accelerating. By June 30, ESG mutual and exchange-traded funds had already drawn double the amount of last year's $5.5 billion of net new money, according to **Morningstar Inc.**

However, 401(k) plan adoption **remains low.** Only 4% of 401(k) plans have an ESG fund available for investment by plan participants, and ESG funds only hold 0.03% of 401(k) assets, according to the Plan Sponsor Council of America.

North American institutional investors, such as pension funds, foundations and endowments, said fiduciary duty was the most significant factor in their ESG adoption, with 59% of institutions' senior investment executives identifying it as such, according to a **survey report** published this month by **State Street Global Advisors**.

In September, the University of California announced it was divesting its $13.4 billion endowment and $70 billion pension from all fossil-fuel investments.

"We believe hanging on to fossil fuel assets is a financial risk," Jagdeep Singh Bachher, the university's chief investment officer, and Richard Sherman, chairman of the board of regents' investments committee, **wrote** in a *Los Angeles Times* opinion piece.

Federal Reserve officials **recently signaled** the Fed will take a more proactive approach in studying how global warming and climate risk pose threats to the financial system and economic stability.

Importantly, ERISA doesn't have a legal list of required considerations for plan fiduciaries — it defers to the judgment of fiduciaries overseeing 401(k) investments, attorneys said.

"It would be unusual for a court to pull any one factor [such as climate] out and all of a sudden make it a required factor," Mr. Oringer said. "And I think more unusual still is when the factor in question is an emerging, new concept."

However, he conceded that it's impossible to know how the landscape may change in a few years' time and what considerations may become standard.

Michael Young, manager of education programs at the Forum for Sustainable and Responsible Investment, agreed that a legal case related to climate change in the current environment would likely prove challenging.

"Unless there's a regulatory framework that makes the data more transparent and defines the risk, it's hard to imagine someone being liable for an undefined risk," Mr. Young said.

"That said, I'd like for someone to bring that case forward and see what came out of it," he added.

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