Does the Recently Amended Investment Duties Regulation Change How Fiduciaries Are Expected to Make Investment Decisions for Employee Benefit Plans?

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The more things change the more they stay the same. Or do they? This question should be on every employee benefit plan fiduciary's mind after January 12, 2021, when an amended U.S. Department of Labor ("DOL") regulation went into effect changing the standards under which fiduciaries are expected to make investment decisions for ERISA employee benefit plans. The implemented final rule, however, is notable as much for what it does *not* do as for what it does. The amended regulation that the DOL had proposed on June 30, 2020 was centered on new standards for consideration of environmental, social, and corporate governance factors—referred to as "ESG" factors—in connection with employee benefit plan investing. The DOL received over 8,700 comments in response, in which mutual fund companies, unions, law firms, and academics argued that the proposed regulation was deeply flawed. Some of the critics argued that the proposal improperly discouraged benefit plan investing in vehicles with ESG goals or objectives; others claimed that it improperly created higher standards for fiduciary consideration of ESG factors in evaluating investment options.

After the tidal wave of criticism, the DOL issued a final rule that eliminated all overt references to consideration of ESG factors. Eliminating references to ESG factors altered the nature of the proposed amendment. The regulation left standing instead changes how *all* fiduciaries are to approach *all* investment decision-making in connection with *all* types of employee benefit plans. Under the new rule, fiduciaries are instructed to make investment decisions by considering only "pecuniary" factors, as defined by the DOL, to the exclusion of "non-pecuniary" factors, with limited exceptions. The new standard adopts the idea that loyalty to plan interests requires the exclusion of any other interest, including collateral benefits or goals of an investment, which could include ESG factors.

While the rule itself is stark, its preamble adopts a looser interpretation of what can be considered "pecuniary" factors. Furthermore, the rule weaves in guidance previously published by both Democratic and Republican administrations and does not prohibit fiduciary selection of investments with collateral benefits or ESG goals so long as the selection is based solely on "pecuniary" factors as defined in the final rule, or in compliance with an exception.

On his first day in office President Biden signaled that his administration will review the final rule on Investment Duties as part of his Executive Order on "Protecting Public Health and the Environment and Restoring Science to Tackle the Climate Crisis." It will be interesting to see whether the Biden administration is interested in changing the amended rule itself or just massaging the interpretation, and whether the DOL will explicitly embrace consideration of ESG factors in employee benefit plan investing or leave the amended regulation alone after all. As explained further below, the final rule's changes to existing guidance are nuanced, and allow for benefit plan fiduciaries to consider all types of investments, including ESG focused vehicles, albeit through a narrower lens.

In the end, the final rule on investment decision making that emerged from the filter of constituent comments does not prohibit fiduciaries of ERISA employee benefit plans from selecting investments that have ESG or other collateral objectives or benefits, and does not create different standards for consideration of such investment options. Rather, the amended regulation requires that fiduciaries make investment choices based on consideration of pecuniary factors, which is consistent with the DOL's existing guidance. The final rule does, however, shift focus from considering investment options under the totality of the facts and circumstances to considering only defined pecuniary factors to the exclusion of non-pecuniary factors. This could be a distinction without a difference, however, given the expanded interpretation in the preamble and the flexibility incorporated into the final regulatory language.

The Biden Administration flagged this rule for review. Given that the slimmer final rule is no longer the stranglehold on ESG investing that the original proposal had been, the Biden Administration could decide not to expend its resources changing it. Instead, it could opt for reminding benefit plan fiduciaries that, despite the prior administration's efforts, the DOL does not restrict fiduciary consideration of relevant factors in selecting investments for employee benefit plans, including when considering investment vehicles with ESG or other collateral benefits or goals.

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