

ESG Update: Reactions to DOL Final Rule

In December of last year, we published an article detailing the DOL's **Final Rule** regarding regulations governing plan investment selections, especially regarding consideration of investments focused on environmental, social, and governance issued (ESG). The final rule has sparked reactions in a number of spheres — including two Congressional responses and at least two legal challenges.

A Refresher: The Final Rule

The final rule does not change the basic ERISA principles in this area, but it includes some important changes. The final rule stresses that plan fiduciaries must focus on financial objectives in evaluating plan investment options by running risk-return analyses. Such analyses *may* include consideration of ESG factors, but only to the extent the plan fiduciary determines they are relevant to the risk-return analysis. The final rule is intended to offer a more neutral path between an earlier proposed rule under the current administration (which provided in part that ESG factors would *often* be relevant to risk-return analyses) and with the prior rules under the Trump administration (which placed more constraints on consideration of ESG factors).

Congressional Response

The Congressional response has been largely split along party lines, with Republicans generally voting to nullify the rule and Democrats generally voting to codify the rule. On February 7th, Republican members of both the House and the Senate introduced measures to nullify the DOL's final rule under the Congressional Review Act. The measure passed the House and the Senate in late February and early March. President Biden **vetoed the measure** on March 20, 2023, noting that the measure, if adopted, would have “force[d] retirement managers to ignore ... relevant risk factors” and “prevent[ed] retirement plan fiduciaries from taking into account factors, such as the physical risks of climate change or poor corporate governance, that could affect investment returns.” In late February, House Democrats introduced legislation to amend ERISA to codify certain provisions of the final rule. This

act — the “Freedom to Invest in a Sustainable Future Act” — would make it clear that ESG factors may be included

in consideration of investment outcomes and that ESG factors could be used as tiebreakers when comparing two investments with otherwise equal risk-return profiles. Though there is some chance of this passing the Senate, there is almost no chance of this passing the House. The act has been referred to the House Committee on Education and the Workforce.



Suits Filed

The final rule has been met with at least two legal challenges, both alleging that the final rule violates the Administrative Procedure Act and should be blocked by the court. The first, *State of Utah et. al. v. Walsh et. al.*, was brought jointly by a coalition of twenty-five Republican state attorneys and three private plaintiffs against the DOL. The second, *Braun et. al. v. Walsh et. al.*, was brought by two private individuals who are participants in ERISA retirement plans.

Next Steps

You and your TPA partner may receive questions about these reactions to the final rule. Despite the many challenges explored in this article, the final rule remains in effect and should be followed carefully by plan fiduciaries.

Reminders

- **June 30, 2023:** Deadline for corrective distributions to HCEs for failed ADP/ACP tests for EACA retirement plans.
- **July 29, 2023:** SMMs due for changes in prior year (unless SPD has been updated to incorporate change).
- **July 31, 2023:** Form 5500 due for calendar-year plans.



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