Proposed legislation would allow ESG funds as default in 401(k) plans

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MarketWatch Blog by Alicia H. Munnell

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This change would do nothing but siphon money from workers to Wall Street

Before describing the proposed legislation, let me be clear. I think that climate change is a serious issue and would be happy to pay more in taxes to discourage carbon emissions, to undertake major investments in energy R&D, and to enable the government to address climate change as a major priority.

But I think it is preposterous to suggest that a challenge of this magnitude can be addressed through stock picking. In my view, ESG (Environmental, Social, and Governance) funds are a marketing ploy by financial services firms to repackage actively managed investments – which were becoming increasingly less appealing – in a trendy wrapper. They're expensive and accomplish nothing. And they divert people's attention from the real work that needs to be done to achieve social change.

Thus, I find the **Financial Factors in Selecting Retirement Plan Investment Act** recently introduced by U.S. Sens. Patty Murray (D-WA) and Tina Smith (D-MN) and Rep. Suzan DelBene (D-WA) very troubling.

The legislation would:

- amend ERISA to permit fiduciaries to account for ESG factors when selecting investments for ERISA-covered retirement plans;
- permit fiduciaries to consider ESG considerations as tie-breakers in the case of competing investments;
- eliminate the need for additional documentation in the case of ESG investments;
- allow ESG investments to serve as "qualified default investment alternatives" (QDIA); and
- rescind the Department of Labor's 2020 ***Financial Factors*** rule, which prohibited fiduciaries from investing in "non-pecuniary" vehicles that sacrifice investment returns or take on additional risk and outright prohibited them as a default.

For most workers, their only retirement saving occurs in a 401(k) plan, so it's essential that the plan's offerings be prudent investments. The problem is that once an asset manager begins the business of picking stocks, the price goes up. And **study after study** over decades has shown that, on average, active managers do not produce the returns to cover these fees.

That is not to say that some firms have not been successful. If a particular actively managed fund – ESG or not – has a solid track record, it could be included in the lineup. But ESG funds should not face a lower hurdle than other investments.

Most importantly, high-fee ESG funds should not be the default. Such an arrangement would not eliminate a thimbleful of greenhouse gases but rather would simply siphon money from workers to Wall Street.