

## Attachment G



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## MEMORANDUM

TO: Jay Huish  
Executive Director

FROM: Katharine Hobin Porter   
Deputy City Attorney

DATE: January 15, 2016

RE: Summary of Recent DOL Guidance regarding "Economically Targeted Investments"

From time to time, the San Francisco City and County Employees' Retirement System ("SFERS") considers potential investments and investment policies based on socially responsible or other similar investing principles and the question is whether those principles are consistent with SFERS' fiduciary duties in administering the plan. In October 2015 the U.S. Department of Labor ("DOL") issued Interpretive Bulletin 2015-1 ("IB 2015-1"), a copy of which is attached to this memorandum. In IB 2015-1 the DOL updates its guidance on the fiduciary duty under the Employee Retirement Income Security Act of 1974, as amended ("ERISA") for decisions to invest plan assets in "economically targeted investments" ("ETIs"). Although SFERS is not covered by ERISA, laws, rules and regulations under ERISA often serve as a model or best practice for non-ERISA pension plans. In this memorandum, we summarize the DOL's guidance to fiduciaries in IB 2015-1, which SFERS could look to as it may consider proposals to invest in ETIs.

### Provides definition of ETIs.

As defined in IB 2015-1, ETIs are "investments selected for the economic benefits they create apart from their investment return to the employee benefit plan." (IB 2015-1, p. 9.) In IB 2015-1 the DOL recognizes the term has wide application and that there is no uniform meaning or terminology to capture this concept, and other terms such as "socially responsible investing," "sustainable and responsible investing," "environments, social and governance investing," and "impact investing" are all used in connection with investments selected because of the collateral economic or social benefits they may advance, in addition to their investment returns.

### IB 2015-1 replaces the 2008 guidance, and restates the 1994 guidance.

The DOL had previously addressed ETI investment issues with Interpretive Bulletins in 1994 and 2008. In IB 2015-1, the DOL expressed concern that the 2008 guidance had "unduly discouraged" fiduciaries from considering ETIs and environmental, social and governance ("ESG") factors. In the 2008 Interpretive Bulletin the DOL had noted that fiduciaries should contemporaneously document their economic analysis of ETIs to show that the investments were equal. IB 2015-1 clarifies that no special or additional documentation is required for ETIs or

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consideration of ESG factors. But fiduciaries still should maintain records sufficient to demonstrate their compliance with fiduciary standards. (See IB 2015-1, p. 5, p. 7.)

Restates the basic fiduciary rule and identifies two scenarios in which plan fiduciaries may take ETI considerations into account in making investment decisions.

In IB 2015-1 the DOL recognizes the basic fiduciary rule under ERISA: a fiduciary must act prudently and solely in the interest of the plan and its members and beneficiaries. In making an investment or engaging in an investment course of action, fiduciaries must give appropriate consideration to relevant facts and circumstances, for example, diversification, liquidity, risk and return, and alternative investments with similar risk and return profiles. A fiduciary must not subordinate the interests of the plan and its members to unrelated objectives, or sacrifice the economic interests of a plan to promote collateral benefits. The focus of plan fiduciaries on a plan’s financial returns and risks to members and beneficiaries must be paramount. “Under ERISA, the plan trustee or other investing fiduciary may not use plan assets to promote environmental, social, governance or other public policy causes at the expense of the financial interests of the plan’s participants and beneficiaries. Fiduciaries may not accept lower expected returns or take greater risks in order to secure collateral benefits.” (IB 2015-1, p. 3.)

At the same time, in IB 2015-1 the DOL confirms its consistent view that fiduciaries may take considerations associated with ETIs, including ESG factors, into account as “tie-breakers” when investments are otherwise equal with respect to return and risk over the appropriate time horizon. (See IB 2015-1, p. 6.)

Also, an “important purpose” of IB 2015-1 is to clarify that ESG factors “may have a direct relationship to the economic value of [a] plan’s investment.” (IB 2015-1, p. 7, emphasis added.) When they do, these factors are more than just collateral considerations or tie-breakers, but rather are “proper components of the fiduciary’s primary analysis of the economic merits of competing investment choices...” (IB 2015-1, p. 6.) “Fiduciaries need not treat commercially reasonable investments as inherently suspect or in need of special scrutiny merely because they take into consideration [ESG] or other such factors.” (IB 2015-1, p. 6.)

In summary, IB 2015-1 provides that the “fiduciary standards applicable to ETIs are no different than the standards applicable to plan investments generally.” (IB 2015-1, p. 10.) And fiduciaries must continue to rigorously review and evaluate all potential investment options – including ETIs.