

# Responsible Retirement: A Toolkit for 401(k) Plan Fiduciaries

## INTRODUCTION

For many plan advisors and consultants, company retirement plan committees, and other fiduciaries (collectively, plan fiduciaries), navigating the rising demand for sustainable investment products—in addition to the widely accepted norm that prudent investors will consider climate risks, and other environmental, social and governance (ESG) factors in 401(k) and similar plans—while adhering to fiduciary duties can feel like a big undertaking.

We have compiled this collection of resources to help prepare you to meet your fiduciary obligations, offer your plan participants responsible fund options, and ensure that all your plan’s investment choices address relevant financial risks and opportunities.

Climate, human rights violations, water shortages, and biodiversity losses are financial risks to individual companies, investment portfolios, and the global economy. Ceres and many experts believe that plan fiduciaries should consider these risks in their investment choices, from the plan sponsor to the portfolio manager. Plan participants who seek to mitigate climate and sustainability risks and capitalize on related opportunities want access to sustainability-themed or other responsible investment choices that could include, but are not limited to, screened funds, responsible index funds, or funds managed to achieve high investment performance and sustainability performance.

A key component of 401(k) plans is the ability of individual participants to decide how they invest their retirement savings. However, retirement plan fiduciaries determine the limited menu of options from which participants can choose. Despite demand for sustainable fund choices, [fewer than 5% of plans](#) currently offer those sustainable investing options.

On January 30, 2023, the U.S. Department of Labor’s (DOL) final rule, [Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights](#), took effect, and is widely recognized as a return to neutrality—that is, neither for nor against consideration of ESG factors in investment decision-making. The rule clarifies that fiduciaries under the Employee Retirement Income Security Act (ERISA) may consider any factors relevant to investment risk and return, including the economic effects of climate change, when making investment decisions.

Key elements of the rule include:

- clarifies that plan fiduciaries who take participants’ preferences into account do not violate the duty of loyalty ([87 FR 73842](#)).
- removes a perceived prohibition on using ESG funds as plan defaults, known as Qualified Default Investment Alternatives (QDIAs), and provides additional clarification regarding the use of QDIAs ([87 FR 73861](#)).
- allows fiduciaries to consider collateral benefits, such as the consideration of environmental impacts for nonfinancial objectives, in a tiebreaker between financially equivalent options ([87 FR 73860](#)).

- does not mandate, prohibit, encourage, or discourage any particular type of investment so long as fiduciary duties are met ([87 FR 73854](#)).
- reaffirms that fiduciary duty includes the management of shareholder rights such as proxy voting ([87 FR 73844](#)).

These provisions make clear that ESG considerations can be relevant to a risk-return analysis and be used to maximize participant returns. As noted above, a sustainable investment choice can even be [considered as the plan's default fund](#), given that it will be subject to the [same prudent process analysis](#) as any other fund for the plan.

A recent court challenge to the rule has been unsuccessful. In September 2023, a district court in Texas ruled in favor of the DOL, stating:

“To summarize, an ESG factor could be worth consideration even under prior rules if it ‘is expected to have a material effect on the risk and/or return of an investment.’ 85 Fed. Reg. At 72884. Similarly, the 2022 Rule states that risk and return factors may include ESG factors under some circumstances, but those factors must still reflect ‘a reasonable assessment of its impact on risk-return.’ 29 C.F.R. § 2550.404a-1 (b)(4). In other words, the 2022 Rule ‘provides that where a fiduciary reasonably determines that an investment strategy will maximize risk-adjusted returns, a fiduciary may pursue the strategy, whether pro-ESG, anti-ESG, or entirely unrelated to ESG.’ ECF No. 88 at 13- 14.” ([Memorandum Opinion, Utah v. Walsh](#))

As a plan fiduciary, your familiarity with the DOL’s regulation is important. It should bring peace of mind that the core principles of ERISA have not changed over many years. With that knowledge in hand, the next step is understanding how climate and sustainability fit into a retirement plan and why they deserve a place in your analysis.

First, you can acquaint yourself with the terminology in use to define sustainable investing. The [CFA Institute](#) has defined five terms used in responsible investing approaches that will help you understand the potential fund strategies available. Additionally, many groups have categorized sustainable funds with terms like integration and focused or themed. Some examples include [The Wagner Law Group](#), the [Defined Contribution Institutional Investment Association](#) (DCIIA), and even a [2022 SEC rule proposal](#). Names and categories are helpful to navigate the market of available funds, but your own due diligence on financial and sustainability performance will be the core step of implementation.

Second, let’s dive into the resources in this toolkit.

Part 1: The **Resource Library** will help you locate existing resources covering major topic areas from regulation to fund evaluation to implementation.

Part 2: The **Engagement Tool** section offers an actionable guide for engaging your service providers on climate and sustainability.

Part 3: The **Expert Perspective** offers a Q&A with ERISA expert, thought leader, and founding partner of Endeavor Law, Bonnie Treichel, on what effective implementation of sustainability in a retirement plan can look like.

# Resource Library

## ABOUT THE REGULATIONS

The following resources can help you get an overview of DOL's "Prudence and Loyalty" rule from a legal perspective and understand how sustainable funds are applicable under ERISA:

- Legal Alert: [DOL Final Regulation Eases Path for ERISA Fiduciaries to Consider ESG Factors When Selecting Investments](#) (Kirkland & Ellis)
- Legal Alert: [DOL's New Rule on ERISA Investment Duties and Its Relationship to ESG](#) (Covington)
- Webinar: [Climate and 401\(k\) Plans: The DOL's New Rule Levels the Field for ESG](#) (Ceres)
- Legal Opinion: [ERISA Opinion on Climate-Aligned Fund Options for DC Plans](#) (The Wagner Law Group)

Another regulator has introduced a rule that may impact sustainable funds and the information available about them. The Securities and Exchange Commission (SEC) recently adopted the [Investment Company Names rule](#), which will require funds that suggest a particular investment strategy such as "low carbon" or "ESG" in their name to clearly define that strategy and ensure 80% of the fund's holdings are invested in line with the chosen label.

## IMPACT OF CLIMATE AND OTHER SUSTAINABILITY RISKS ON INVESTMENTS

Natural disasters, water shortages, or human rights violations can all impact a company's profitability and the health of the broader economy. The following reports provide data behind the existing and future risks, which are of import to long-term investors like retirement savers:

- Report: [How sustainability risks affect investments](#) (Nordea)
- Report: [World's biggest companies face \\$1 trillion in climate change risks](#) (CDP)
- Report: [The United States' turning point on climate change: The economic opportunity of climate action in the US](#) (Deloitte)
- Report: [The Carbon Impact of U.S. Company Sponsored 401\(k\) Plans](#) (CFA Institute and Business Climate Finance)

## RESPONSIBLE INVESTING MYTHBUSTERS

Responsible investing strategies [have a long history](#), but misconceptions about performance and applicability in retirement plans have created roadblocks for plan fiduciaries. Below are a few facts and the back-up resources, noting that we are not financial advisors and are not recommending specific funds or investment strategies:

**Responsible investing does not inherently sacrifice performance. Instead, it can lower risk.**

- Study: [Responsible Investing: Delivering competitive performance](#) (Nuveen)

- White Paper: [Sustainable Reality: Analyzing Risks and Returns of Sustainable Funds](#) (Morgan Stanley)
- List of Studies and Resources: [Financial Performance with Sustainable Investing](#) (US SIF)
- List of Studies and Resources: [Financial Performance: Can sustainable investments achieve performance objectives?](#) (Intentional Endowments Network)

**Employees want sustainability-themed or integration fund options and will invest in them when offered.**

- Survey: [2023 Retirement Outlook](#) (MFS)
- Survey: [2022 US Retirement Survey](#) (Schroders)
- Report: [Give the people what they want](#) (Natixis)
- Case Studies: [ESG in Defined Contribution Plans: Increased Participation When Plans Embrace Responsible Investing](#) (Natixis)

**Sustainable funds with proven track records exist across fund categories.**

- White Paper: [The rise of the sustainable fund market and its role in financing sustainable development](#) (UNCTAD)
- Column: [Can Plan Sponsors Include Climate Funds in a 401\(k\)?](#) (Nasdaq)

We highly encourage you to conduct your own research into available fund options. For purposes of example, the following list displays a handful of fund categories and existing funds in those categories that have a sustainability mandate, a track record of five years or more, and an expense ratio below 1% (as of December 8, 2023):

Fund Category	Examples	Track Record
Target Date – Allocation Funds	Natixis Sustainable Future	5+ years
Balance – Allocation Funds	Calvert Balanced Fund	20+ years
	AB Sustainable Thematic Bal Port I	20+ years
Sector Equity Fund	Invesco Water Resources ETF	15+ years
	VanEck Environmental Services ETF	15+ years
U.S. Equity Fund	Parnassus Mid Cap Growth Fund	20+ years
	Amana Mutual Funds Trust Growth Fund	20+ years
International Equity Fund	Impax Global Environmental Markets Instl	15+ years
	Morgan Stanley Institutional Fund, Inc. Global Sustain Portfolio I	10+ years

*The above funds are only examples and should not be construed as investment recommendations or promotions. Data acquired from As You Sow's [Invest Your Values](#).*

# IMPLEMENTATION OF A RESPONSIBLE STRATEGY IN RETIREMENT PLANS

## Existing Toolkits and Guides

Several organizations and retirement consultants offer step-by-step guides to considering sustainability in 401(k)s and similar plans. The following includes both comprehensive toolkits and helpful a la carte tools:

- Comprehensive Toolkit: [Aligning Retirement Assets Toolkit #1: The responsible retirement plan opportunity](#) and [Aligning Retirement Assets Toolkit #2: United States Version](#) (WBCSD)
- Brief Guide: [How to approach ESG with plan committees](#) (Nuveen)
- Legal Opinion: [ERISA Opinion on Climate-Aligned Fund Options for DC Plans](#) (The Wagner Law Group) — Exhibit B: Sample Fiduciary Procedural Checklist
- Resource Library: [ESG Research Landscape And Resources For DC Plan Sponsors](#) (DCIIA)
- Glossary: [Sustainable Fund](#) (Carbon Collective)

## Fund and Company Evaluation Tools

Systems for analyzing and rating ESG funds exist across numerous platforms. The following are free tools that report on both the impact and financial performance of funds:

- [As You Sow's Invest Your Values](#): This tool assesses both large existing 401(k) plans and individual funds. At the fund level, you can view a scorecard of ESG indicators and high-level financial performance provided by Morningstar.
- [MSCI's ESG Fund Ratings](#): This tool allows you to look up individual funds and explore how the fund aligns with various criteria established by MSCI including global climate goals, climate transition risks and opportunities, ESG score, and more. MSCI also offers a [tool to look up public companies](#) and explore ratings on similar criteria.
- [InfluenceMap Asset Managers & Climate Change 2023](#): This report scores asset managers on climate stewardship, portfolio alignment with the Paris Agreement, fossil fuel investing, and policy advocacy.

## Examples of Implementation

What does the inclusion of climate and sustainability factors actually look in a 401(k) plan? While it can look different for every company, these two examples can help you visualize the options:

- Sample Portfolio Construction: [ESG 401\(k\) Portfolios](#) (Carbon Collective)
- Case Study: [Optimizing Returns and Supporting Company Values Through Sustainable Investing](#) (Accounting for Sustainability)

## Perspectives on Investment Policy Statement and Sample Sustainability Language

Your investment committee may consider updating its Investment Policy Statement (IPS). Consult your legal team on how to proceed. Need inspiration? Here are a few samples of language:

- Guide: [Incorporating ESG in DC Plans](#) (DCIIA) — Page 4
- Webinar: [The Door Is Open... Wider: ESG Investing for Retirement Plans](#) (Wealthmanagement.com) — At 35:20
- Legal Opinion: [ERISA Opinion on Climate-Aligned Fund Options for DC Plans](#) (The Wagner Law Group) — Exhibit A: Sample IPS Addendum

## The Role of the Qualified Default Investment Alternative (QDIA)

Most retirement participants hold their funds in a QDIA, so the shortest route for participants to mitigate climate and sustainability risks in their investments is to [offer a responsible default fund](#). The following resources review ESG funds as QDIAs, participant behavior, and new funds in the market.

- Brief Guide: [Evaluating ESG funds: A fiduciary's guide to navigating some of the more complex circumstances](#) (Vanguard)
- Report: [How America Saves 2023](#) (Vanguard) — Page 72
- News: [Major Players Offer New Sustainable ESG Target Date Funds](#) (NAPA)

## Recommendations for Participant Education on Sustainable Funds

A lack of participant awareness and understanding can be a barrier to increasing assets in sustainability-focused investment options once added to a plan. In addition to updating plan documents, work with your service providers to plan for education and participant outreach:

- Presentation: [ESG and Participant Communications: Practical ideas for how to communicate the integration of sustainable investing within DC plans](#) (DCIIA)
- Column: [Considerations for DC Plan Sponsors Integrating ESG Investments](#) (PlanSponsor)

# Engagement Tool

## Guiding Questions for Your Service Providers

If you are working with an investment advisor/manager, engaging directly with an asset manager, or are a service provider utilizing this kit, you will need to review current plan offerings and criteria for new offerings.

The first step is to gain insight into how climate and other sustainability risks and opportunities are currently addressed in the plan and the capacity for asset managers to offer such options. The questions below can help you initiate a dialogue with your plan advisor or consultant and/or asset

manager about the plan's investments as well as help you establish benchmark criteria for the consideration of new investments.

#### About the Asset Manager

- Does this asset manager have an Investment Policy Statement that defines its approach to managing climate and sustainability-related risks and opportunities?
- Is this asset manager a signatory of the Net Zero Asset Managers (NZAM) initiative? Signatories are listed on the [NZAM website](#).
- Does this asset manager have an [Investor Climate Action Plan \(ICAP\)](#) – or a net zero transition plan – that addresses governance, investment, corporate engagement, policy advocacy, and investor disclosure?
- Does this asset manager offer portfolios with a science-based emissions reduction target in line with 1.5°, interim goals for 2030, and/or global net zero emissions by 2050?

#### About the Funds

- Does this fund's label mention ESG, sustainability, or another term suggesting an investment approach within its portfolio and disclose in its prospectus how the investment approach is applied?
- Does this fund have a sustainability mandate?
- Does this fund regularly include climate and/or other sustainability risk factors in its risk-return analysis?
- Does this fund have an engagement strategy on climate and/or other sustainability issues?
- How are the shares of this fund voted on climate-related and/or other sustainability-related resolutions?

## Expert Perspective

*Bonnie Treichel, JD, is the Founding Partner of Endeavor Law. She is a nationally recognized speaker and thought leader.*

### **How should effective plan fiduciaries optimize climate and other sustainability factors in the retirement plan?**

The Employee Retirement Income Security Act of 1974 (ERISA) is a law of process, not outcomes. ERISA gives broad deference to fiduciaries to follow their process with the information they know (or should know as a prudent fiduciary) at the time and to monitor their investment options and service providers, including investment managers, on an ongoing basis. When selecting and monitoring investments, plan fiduciaries should be mindful of the Department of Labor (DOL) final regulation, which applies to all investment choices. Specifically, this now-effective regulation requires that a fiduciary's determination with respect to any investment be based on a risk and return analysis. It permits – but does not mandate – that such analysis include the economic effects of climate change

and other environmental, social and governance (ESG) factors if the plan fiduciary determines that they are relevant.

For plan fiduciaries that find economic value to either reduce risk or increase return based on climate or other sustainability factors, such analysis should be incorporated into the criteria for selecting and monitoring investment options. This analysis may be based on specific companies or industries where climate and other sustainability factors are relevant. Plan fiduciaries should develop a clear process that identifies which factors they use in their analysis when evaluating investment management firms and investment options, including analysis involving climate and other sustainability factors. Further, they should prescribe this process, including qualitative and quantitative metrics, in an investment policy statement (IPS) (or other stated policy/guidelines), provide periodic (e.g., quarterly) investment reports reflective of the stated metrics, and summarize the process in meeting minutes. Plan fiduciaries may, and even should, include climate or other sustainability factors in these metrics, but only to the degree they are additive to the risk/return analysis.

### **How do plan fiduciaries objectively navigate the various rating tools when conducting an analysis?**

Given that ERISA requires an objective process, it is important for plan fiduciaries to start with an IPS or other stated investment objectives to have a clear understanding of the qualitative and quantitative criteria that will be used to evaluate investment options. The qualitative and quantitative criteria may include climate and other sustainability factors. Plan fiduciaries are encouraged to work with a knowledgeable retirement plan advisor or consultant that can access information about investment options in the following ways:

- meetings with investment managers who are making decisions related to climate and other sustainability factors;
- access to, and understanding, the prospectus for the investment offering; and
- tools and reports based on the data underlying the investment options and the ways they are using ESG factors.

Tools and reports may be the most difficult for plan fiduciaries as they are trying to determine the efficacy of the data underlying such services. For example, as part of the fiduciary obligation, plan fiduciaries should inquire as to the source of the data and understand if the data is derived from reputable, verified sources. This analysis should be combined with existing frameworks for the data and criteria used to select and monitor all investments.

### **What could effective participant education on climate and other sustainability factors look like?**

Many participants may not be aware of the differences in the regulations (and associated duties) for their retirement plan account versus that of their personal investment accounts. For example, it is important to ensure that participants understand that the requirement of the retirement plan is to provide retirement plan investments that are in the best financial interest of all participants. One way to accomplish that financial outcome may be to include climate and other sustainability factors into the analysis so long as those factors are additive to a participant's risk/return outcome.



It may be helpful to assist participants by educating them regarding the following:

- Types of investing and how climate and other sustainability factors may fit into those investment methodologies
- Types of investments in the plan, including helping some participants to understand exposure to ESG investments for which they may not be aware
- Effective resources to learn more about each investment option, including navigating each investment's disclosure (e.g., prospectus)

**How do you suggest plan trustees navigate the desire to keep investment offerings to a reasonable number while providing access to a responsible investing strategy?**

Many defined contribution retirement plans are set-up such that plan fiduciaries find relief from liability under ERISA Section 404(c), which means that plan fiduciaries will be protected from participant selection of investments if a broad range of investments are offered so long as certain requirements are met. A broad range of investments means inclusion of at least three different investment options which have materially different risk and return characteristics. Typically, plan fiduciaries select more than three investment options and may rely upon an investment consultant or advisor to assist with providing recommendations as to which investment options to include in the plan.

Plan fiduciaries should be wary, however, of adding too many investment options. There is research to suggest that when there are too many investment options, participants are unable to engage with the plan, resulting in less engagement and participation. The right balance of enough choice without too much choice is a best practice. This allows for plan fiduciaries to offer a responsible investment strategy that also meets the regulations and doesn't detract from participant engagement.

**DISCLAIMERS**

*This toolkit is prepared for informational and educational purposes only. This information contained herein is deemed to be current and accurate as of the date included, but Ceres is not responsible for ongoing updates to the data or information, including but not limited to, fund information or expense ratios contained herein. The information and recommendations which this toolkit contains do not constitute investment, financial, or legal advice or advice on any other matter. Any references to products, services, or other entities should not be considered a recommendation, endorsement, affiliation, or approval of such product, service or entity by Ceres. Ceres does not assume responsibility for the effectiveness of any programs or plans adopted and implemented by you. Any investment decisions made on the basis of this toolkit are your sole responsibility. This toolkit has been compiled with a variety of external sources believed to be reliable, but Ceres has not verified the accuracy or completeness. While every effort has been made to ensure accuracy, no responsibility can be accepted for errors or omissions within this toolkit.*