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ENVIRONMENTAL LAW • INSTITUTE®

2023 Environmental Law and Policy Annual Review Conference

MARCH 31, 2023
9:30 A.M. - 2:00 P.M.

Analysis of Articles Published in 2021-2022

ELPAR

Environmental Law & Policy Annual Review

2021-2022 Article Analysis

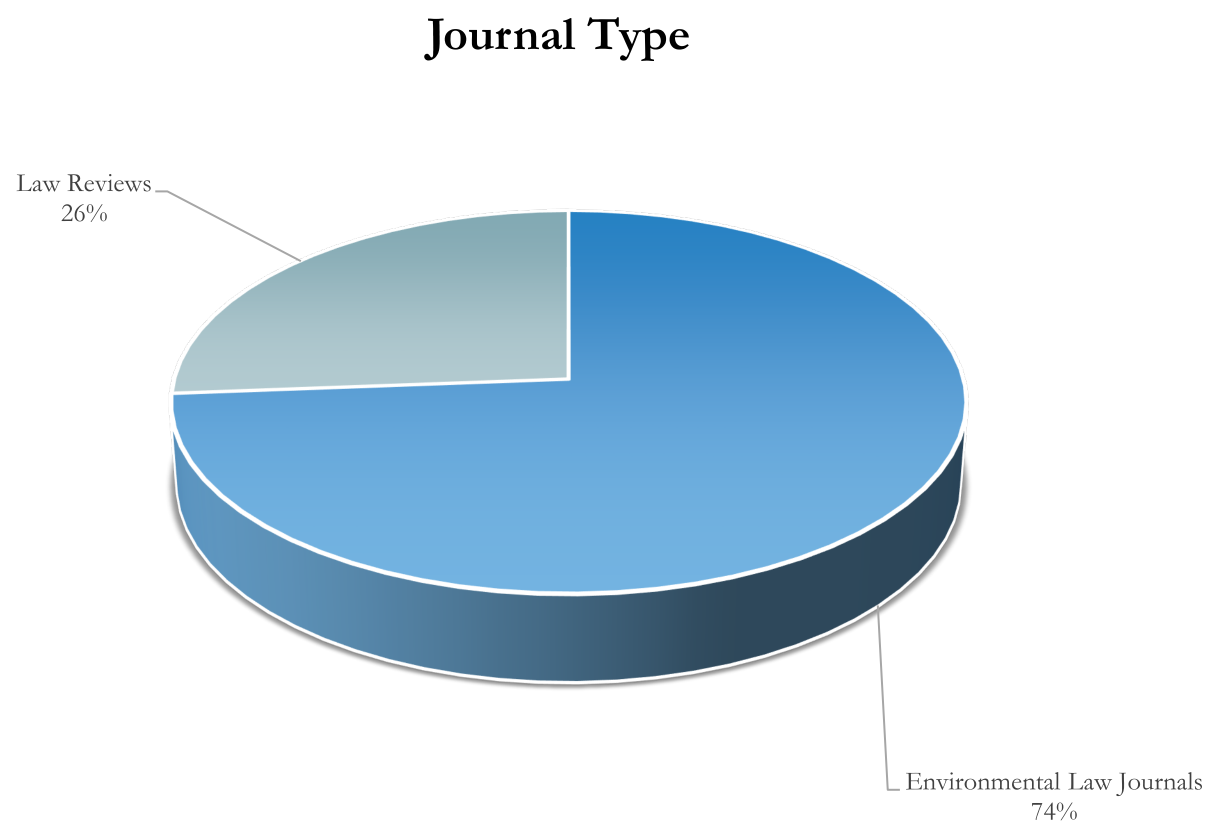
Methodology

- Detailed Methodology:
  - https://www.eli.org/environmental-law-policy-annual-review/publications
- 271 Environmental Law Articles Catalogued

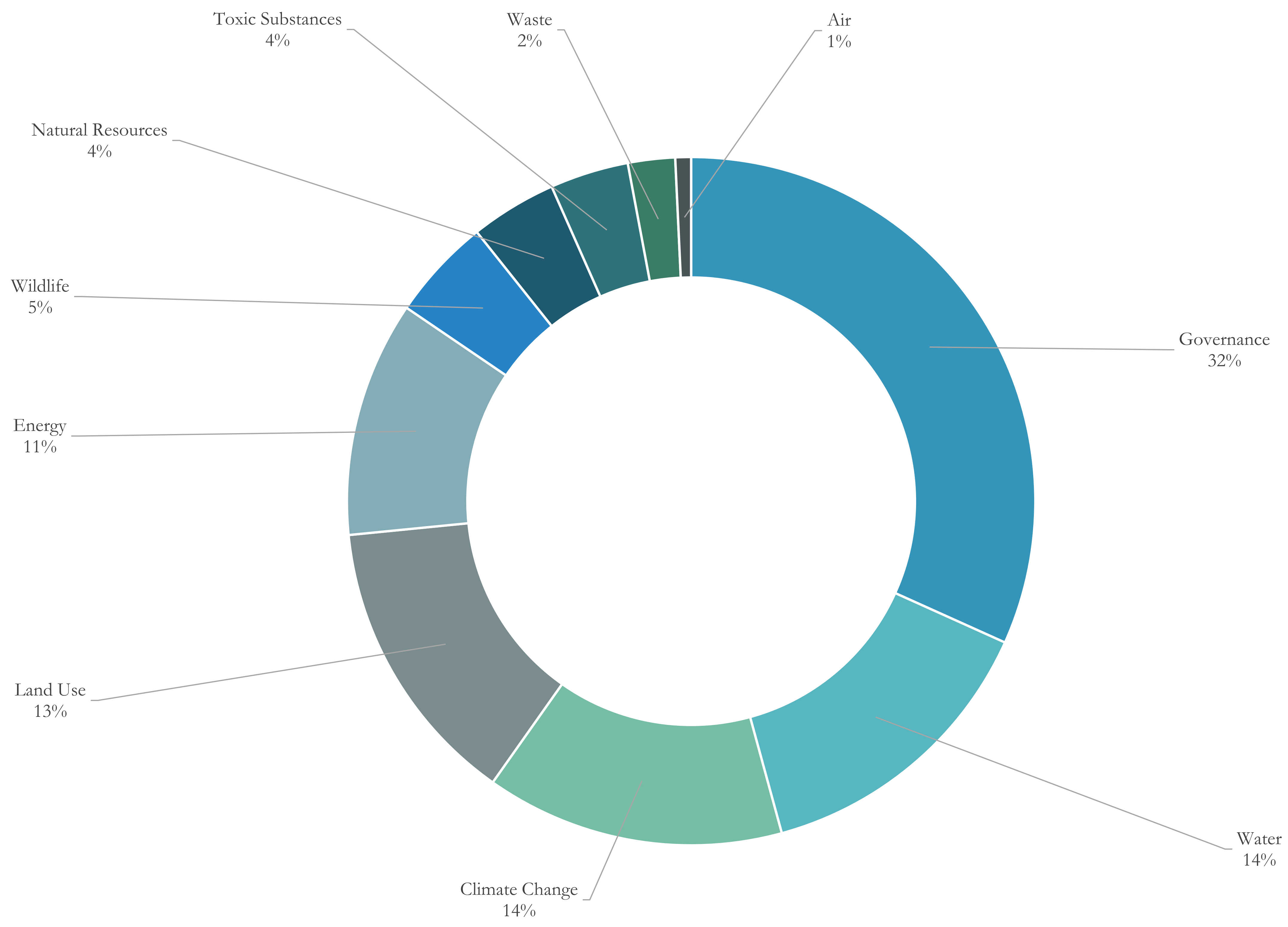
2021-2022 Article Analysis

Environmental Journals vs. General Law Reviews

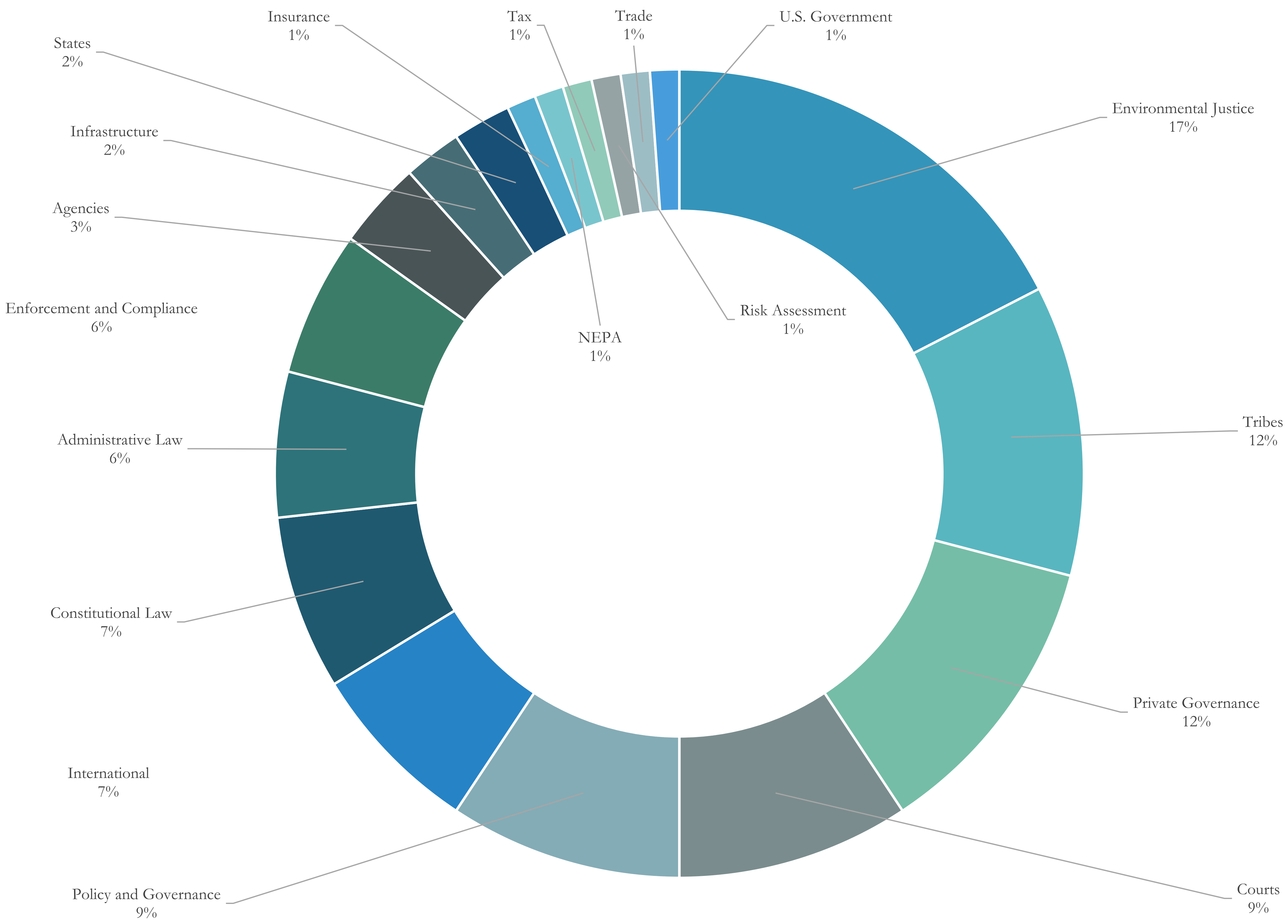
- 271 Environmental Law Articles Catalogued
- General Law Reviews: 71 (26.2%)
- Environmental Law Journals: 200 (73.8%)



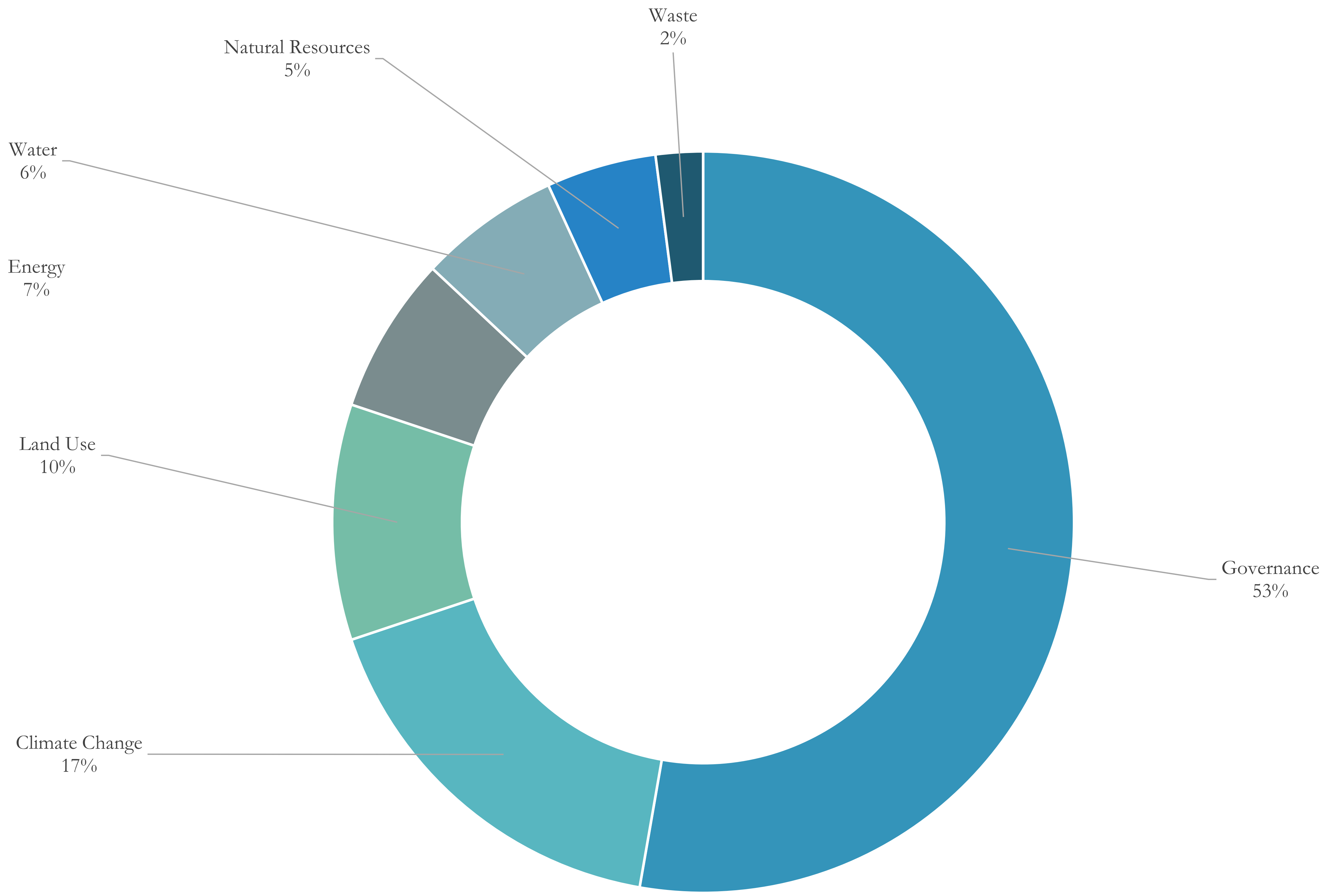
2021-2022 Primary Topics



Governance Sub-Topics



Secondary Topics



Top 20 Article Analysis

Environmental Journals vs. General Law Reviews

- Articles Selected from Environmental Journals: **6**
- Articles Selected from General Law Reviews: **14**

Top 20 Article Analysis

Primary and Secondary Topics

Primary Topics	
Governance	5
Energy	6
Natural Resources	1
Water	1
Climate Change	5
Land Use	2

Secondary Topics	
Governance	5
Climate Change	4
Waste	1
Land Use	1

Top 20 Article Analysis

Policy Proposals

- 5 articles called for federal agencies to promulgate new or updated regulations.
- 5 articles detailed private environmental law solutions.
- 4 articles for updates to federal laws.
- 2 articles for changes in the judicial system by revitalizing old doctrine.
- 2 articles were focused on state or local policy approaches.
- 2 articles called for broad paradigm shifts.

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Comprehensive Environmental and Climate Action Plan (CECAP): Climate Mitigation and Adaptation

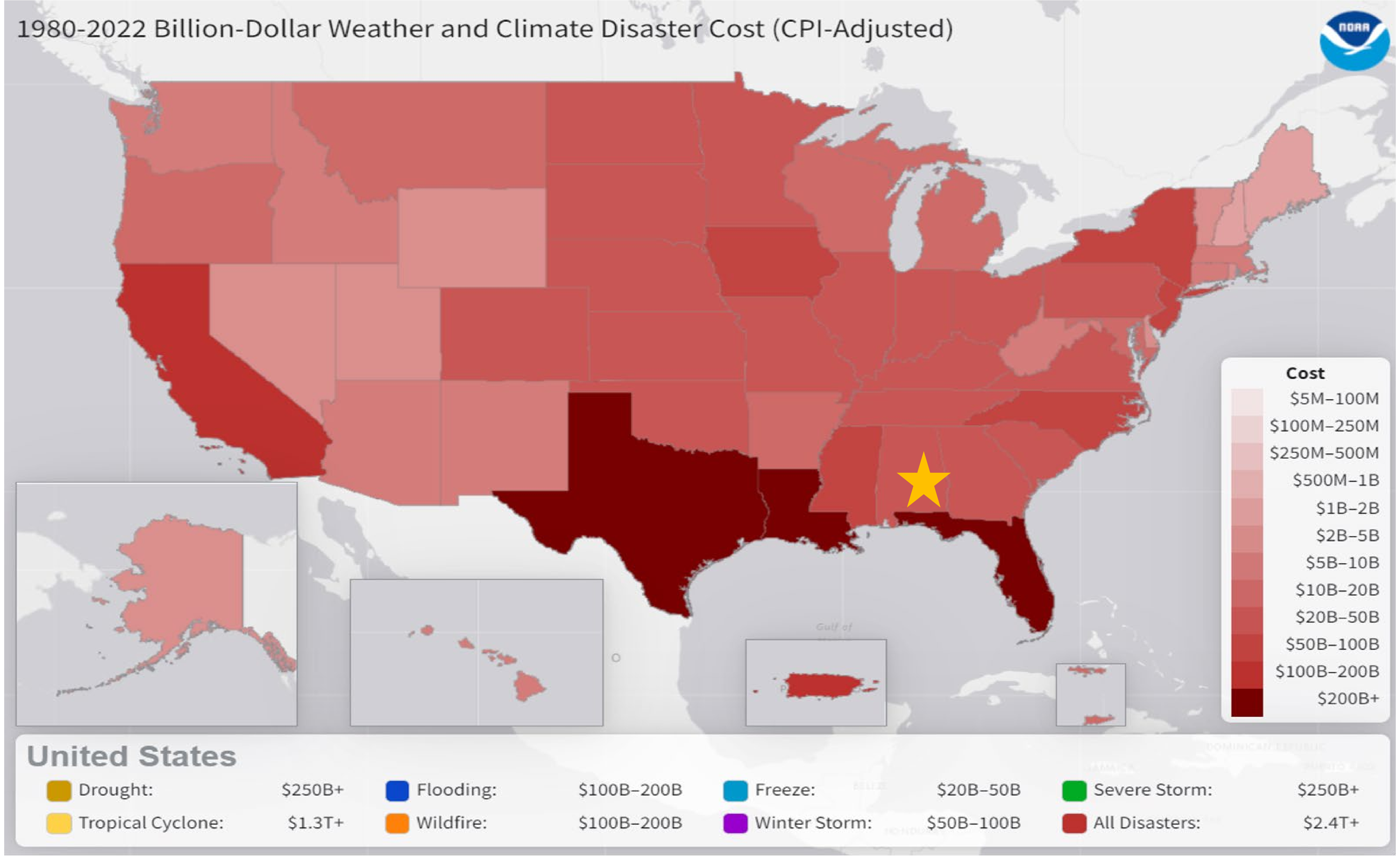
Environmental Law and Policy Annual Review
March 31, 2023

Carlos Evans, Director
Office of Environmental Quality & Sustainability
City of Dallas

Presentation Overview

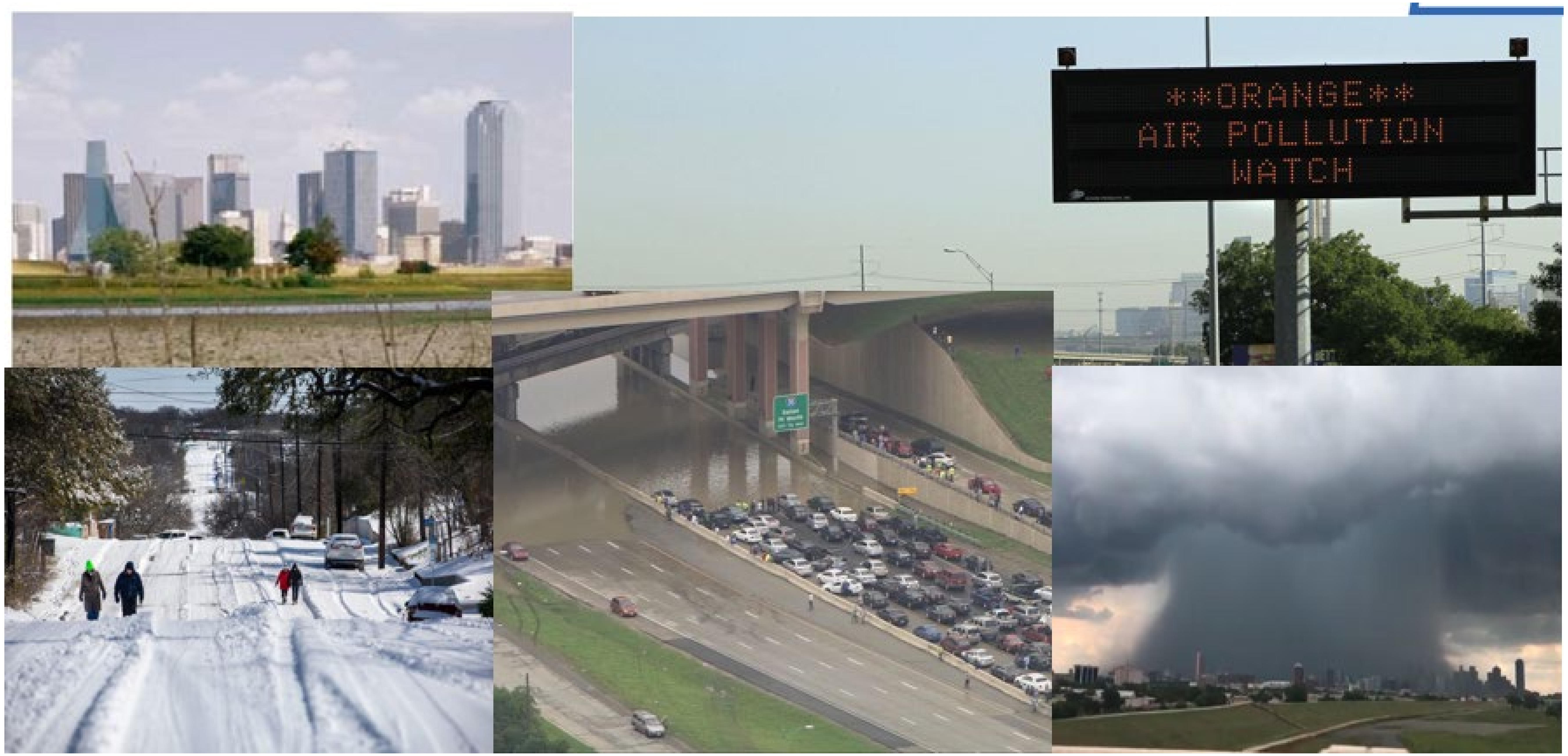
- Background
- Comprehensive Environmental & Climate Action Plan (CECAP) Overview
- Select Mitigation and Adaptation Activities
- Select Climate Legislation/Bills

U.S. Billion-Dollar Weather and Climate Disaster Cost



NOAA National Centers for Environmental Information (NCEI) U.S. Billion-Dollar Weather and Climate Disasters (2023). https://www.ncei.noaa.gov/access/billions/, DOI: 10.25921/stkw-7w73

Environment & Climate Challenges



Domestic Migration & Dallas

"Hurricane Katrina survivors in Dallas offer hard-earned wisdom, support for Harvey evacuees"

- Dallas Morning News (Sept. 1, 2017)

"Family decides to move to Texas after evacuating ahead of Hurricane Ida"

- Spectrum News 1 (Sept. 18, 2021)

Hurricane Katrina

Hurricane Harvey

Comprehensive Environmental & Climate Action Plan (CECAP)

Adopted unanimously by Dallas City Council on **May 27, 2020**

"With equity and inclusion as core values, the CECAP proposes solutions that will improve our natural environment, our education and economic outcomes, the affordability of our housing stock, and our transportation systems."

Mayor Eric Johnson

(8) Eight CECAP Goals

ALL DALLAS' COMMUNITIES BREATHE CLEAN **AIR**.

DALLAS' **BUILDINGS** ARE ENERGY-EFFICIENT AND CLIMATE RESILIENT.

DALLAS GENERATES AND USES RENEWABLE, RELIABLE, AND AFFORDABLE **ENERGY**.

ALL DALLAS' COMMUNITIES HAVE ACCESS TO HEALTHY, LOCAL **FOOD**.

DALLAS PROTECTS AND ENHANCES ITS ECOSYSTEMS, TREES AND **GREEN SPACES** THAT IN TURN IMPROVE PUBLIC HEALTH.

DALLAS' COMMUNITIES HAVE ACCESS TO SUSTAINABLE, AFFORDABLE **TRANSPORTATION** OPTIONS.

DALLAS PROTECTS **WATER RESOURCES** AND ITS COMMUNITIES FROM FLOODING AND DROUGHT.

DALLAS IS A **ZERO WASTE** COMMUNITY.

Striving for 1.5°C

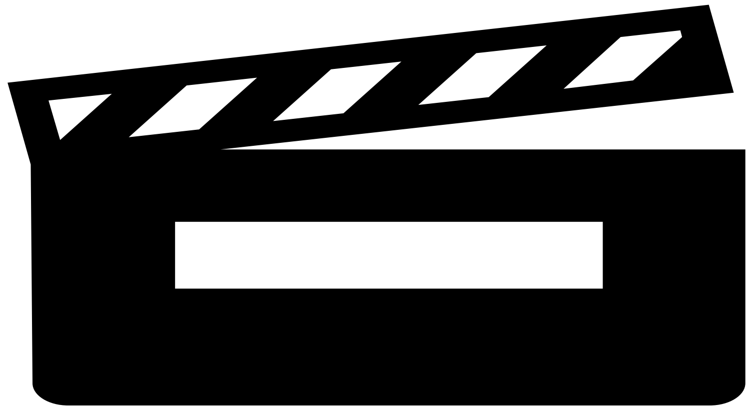
"To avoid the worst impacts, communities across the planet need to ***limit the increase in global temperatures to below 1.5°C****. To achieve this, the* ***Intergovernmental Panel for Climate Change (IPCC) recommends reducing GHG to net zero by 2050****."*

"To position the Dallas CECAP as a climate action plan that meets the ambitious objectives of the ***Paris Agreement****, […]* ***the City of Dallas has adopted a target of carbon neutrality by 2050****."*

\- CECAP

CECAP: 97 Actions

97 CECAP Actions



SECTORS / GOALS	PRIMARY BENEFIT	CO-BENEFITS
16 BUILDINGS	45 MITIGATION	46 IMPROVE PUBLIC HEALTH + WELL-BEING
11 ENERGY	21 ADAPTATION	40 PROVIDE COST SAVINGS
19 TRANSPORTATION	20 ENVIRONMENTAL QUALITY	31 IMPROVE AIR QUALITY
09 SOLID WASTE	11 ENVIRONMENTAL JUSTICE	28 PROVIDE EDUCATION, SKILLS OR TRAINING
15 WATER RESOURCES		24 IMPROVE ACCESS TO EMPLOYMENT / JOB CREATION
09 ECOSYSTEMS		15 REDUCE INEQUALITY + POVERTY
14 FOOD + URBAN AGRICULTURE		17 REDUCE GHG EMISSIONS
04 AIR QUALITY		08 INCREASE NATURAL RESOURCE CONSERVATION
		11 IMPROVE WATER QUALITY
		13 REDUCE RESOURCE CONSUMPTION
		10 PROMOTES ENVIRONMENTAL STEWARDSHIP
		10 REDUCE VULNERABILITY

Building Targets: Dallas' Buildings Are Energy Efficient And Climate Resilient.

TARGETS

Net zero energy new construction

- 100% starting in 2030

Energy use in existing residential buildings

- 10% of existing buildings reduce energy use 10% by 2030
- 10% of existing buildings reduce energy use 25% by 2050

Progress

- **Net Zero Carbon Construction Specs**
  Under evaluation
- **2021 Buildings and Residential Code**
  Require EV Readiness
- **Whole Home Program**
  Implemented
- **Green Job Skills Program**
  Implemented
- **Community Solar & Renewable Energy Bundling Program**
  Under development

Energy Targets: Dallas Generates And Uses Renewable, Reliable And Affordable *Energy*.

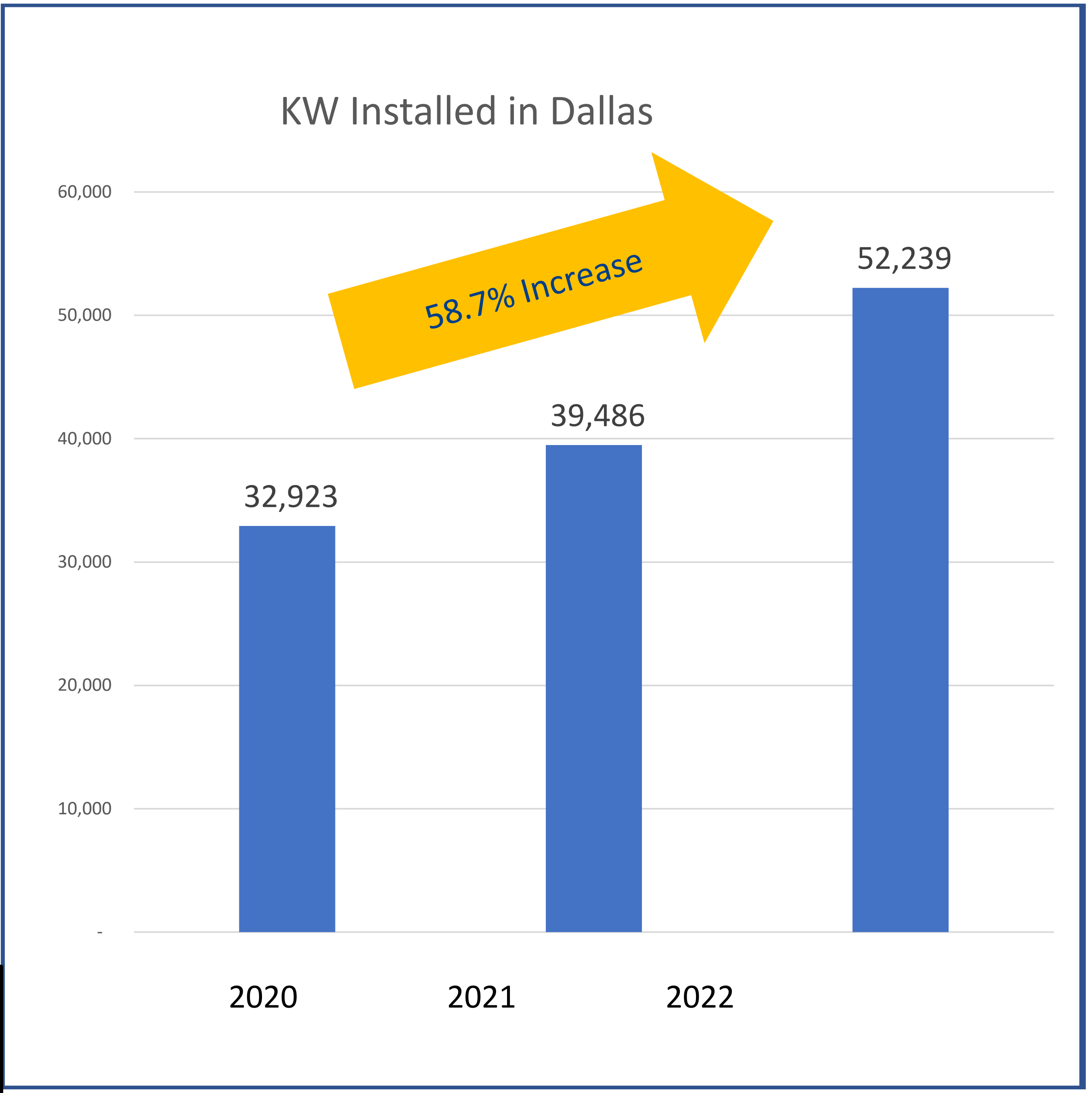
TARGETS

Solar power generated

- 739,000 KW by 2030
- 3,695,000 KW by 2050

Renewable electricity plans

- 20% of residents + businesses enrolled by 2030
- 50% of residents + businesses enrolled by 2050



Data **Sources:** Solar Data: Oncor 2020, 2021 & 2022 Annual Distributed Renewable Energy Report to PUC Residential Renewable Energy data: US Energy Information Administration https://www.eia.gov/energyexplained/use-of-energy/homes.php

Renewable energy sources—geothermal energy, solar energy, and wood fuels—accounted for about **9%** of residential sector energy end use in 2022.

Transportation Targets: Dallas Communities Have Access To Sustainable, Affordable, Transportation Options.

TARGETS

Publicly available EV charging

- 1,500 outlets to support 39,000 vehicles by 2030

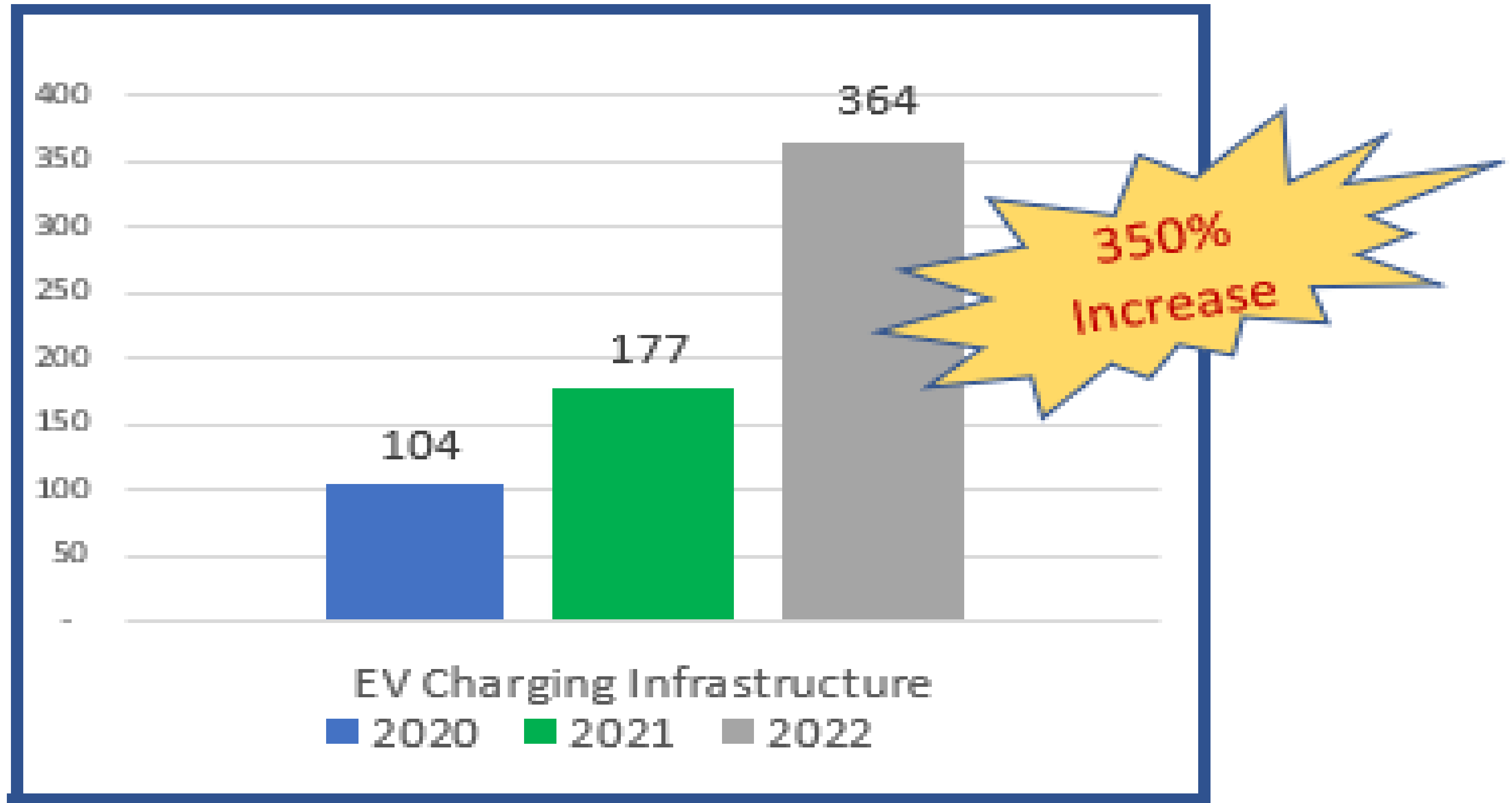
Electric fleets

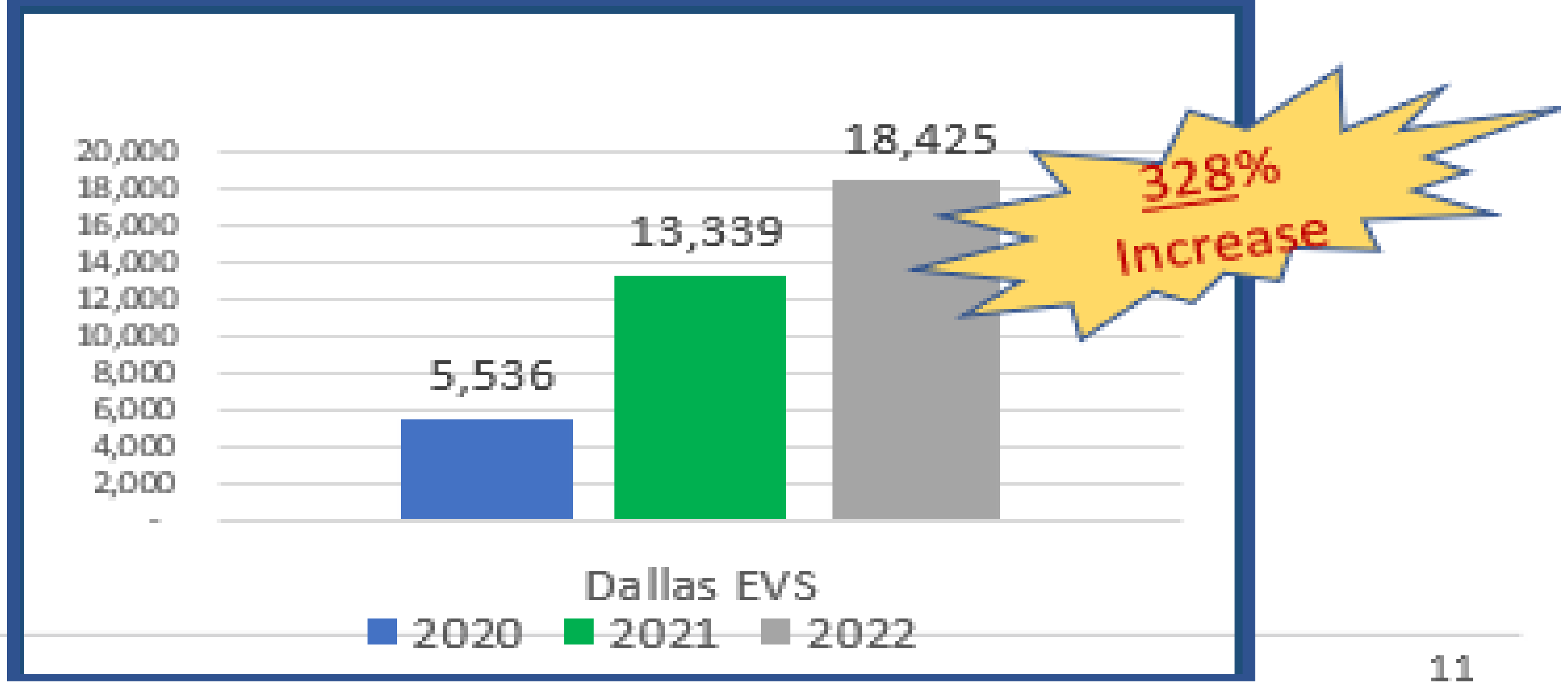
- All new transit vehicle purchases by the City, DISD, and DART fully electric by 2030
- 100% electrified fleet by 2040

Single occupant vehicle travel mode shift

- 88% to 79% in 2030
- 88% to 62% in 2050

Data Source: https://www.dfwcleancities.org/evnt





Water Targets: Dallas Protects Its Water Resources And Its Communities From Flooding And Drought.

TARGETS

Water consumption

- 1% decrease (per-capita) annually

Water for indirect reuse

- 5% implementation by 2030
- 10% implementation by 2050

Impaired waterbodies (303(d) Listed Segments)

- 30%, 60% and 100% reduction by 2030, 2040 and 2050 *(Dallas MS4 Permit Area)*

GHG emissions from treatment facilities

- 45% reduction by 2035
- 100% reduction by 2050

Water Consumption:

10 year rolling average reduction of 1.4%

Select Projects:

Implementing $300 million Mill Creek Stormwater Drainage Project

Implementing Flood Protection Project (Raise and flatten levees; New Pump Stations; New wetlands)

Ecosystem Targets: Dallas Protects And Enhances Its Ecosystems, Trees, And Green Spaces

TARGETS

Canopy cover citywide
- 33% by 2030
- 37% by 2040
- 40+% by 2050

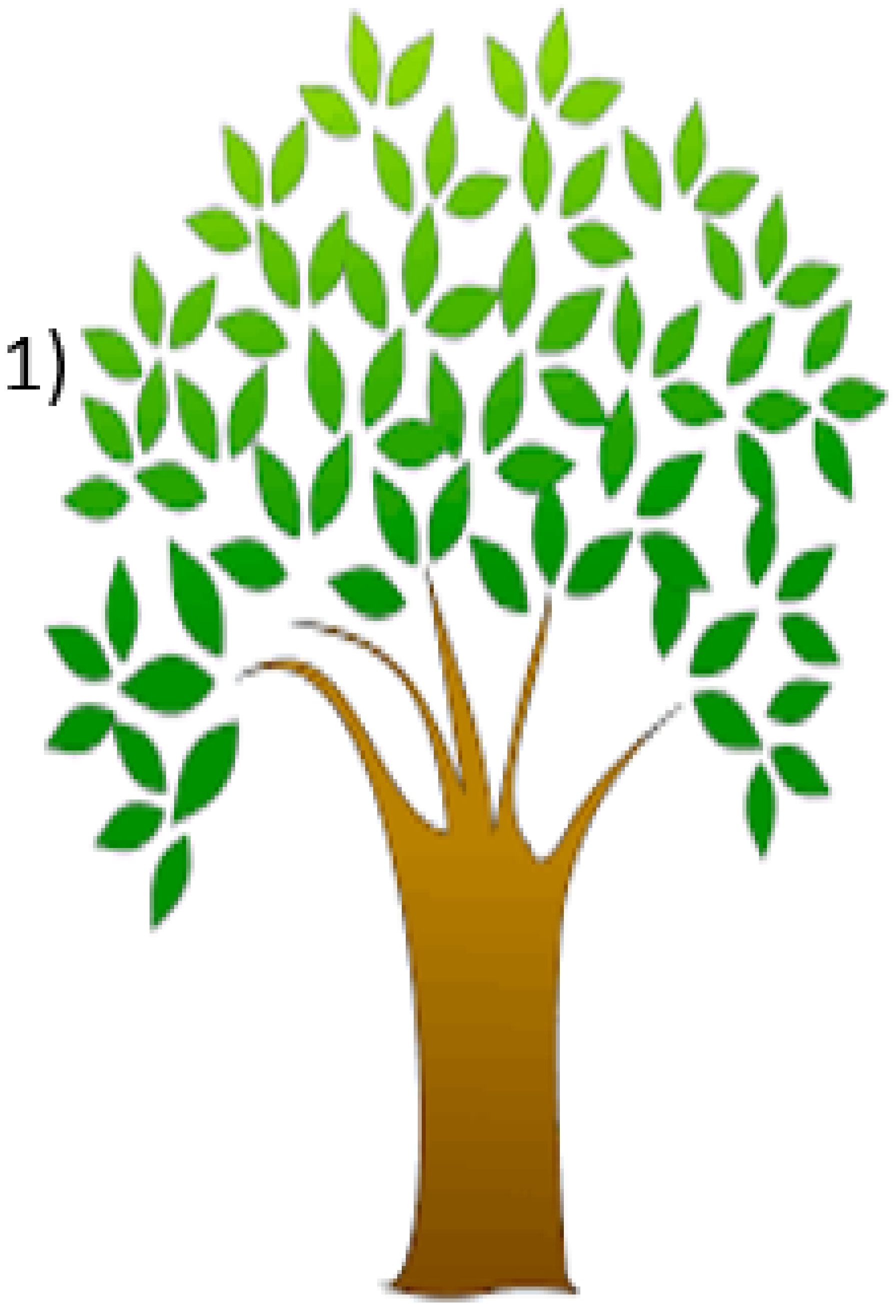
Urban heat island index
- 20% reduction by 2030
- 50% reduction by 2040
- 75% reduction by 2050

Park or trail access *(1/2 mile walk)*
- 80% of the population by 2030
- 90% of the population by 2040
- 95% of the population by 2050

PROGRESS

Tree Canopy
- 193.8 Acres Added + 26.5 acres under design/construction (2021)

Tree Planting
- 10,000 Trees (2021 &2022)



Data Source: Trust for Public Lands

Food Targets: All Dallas Communities Have Access to Healthy, Local Food.

TARGETS

Healthy Affordable Access

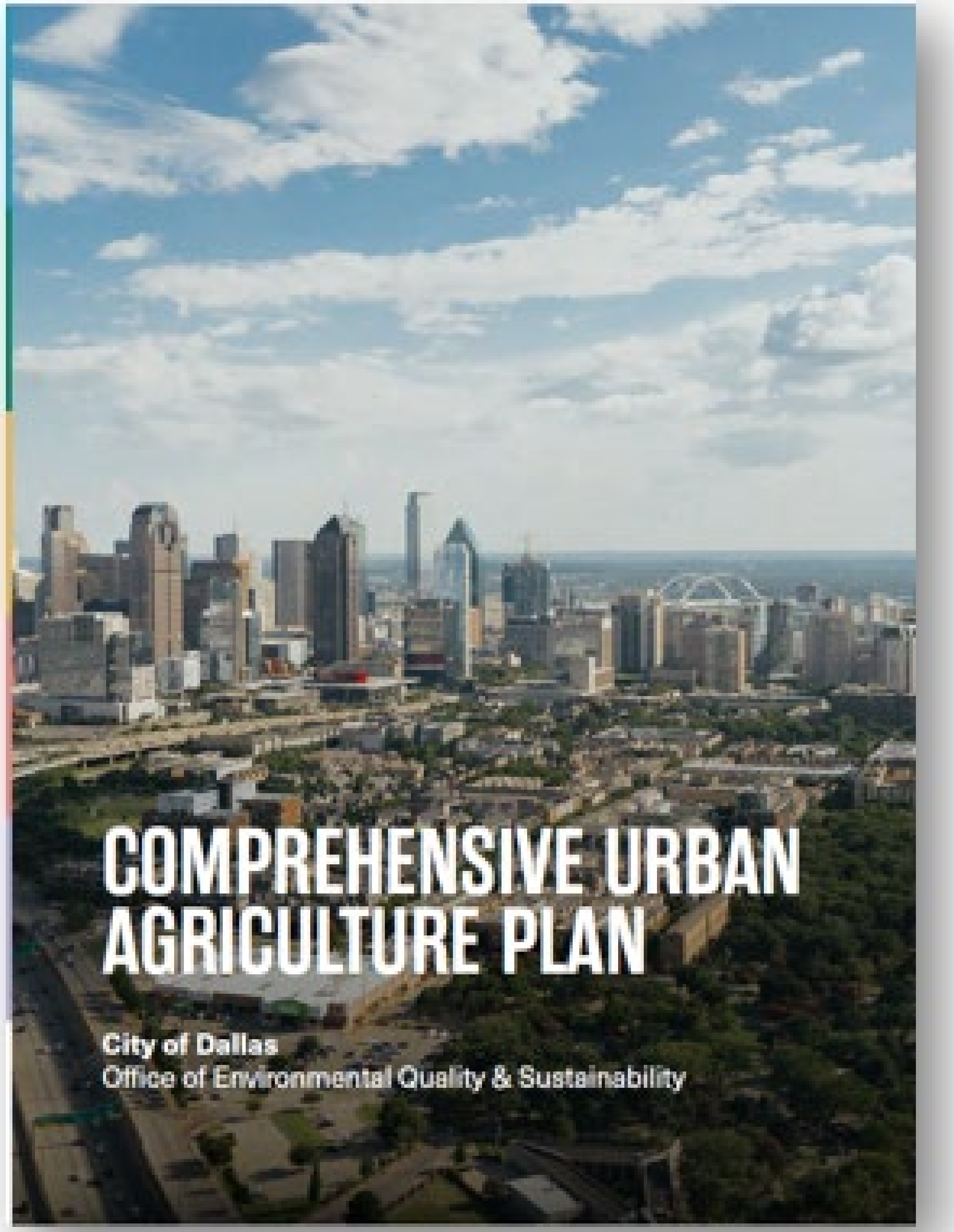
- 50%, 75%,100% of the population lives has access to healthy, affordable food by 2030, 2040, and 2050

Increase urban garden acreage

- Increase by 20%, 50%, 75% the acreage of urban gardens producing food by 2030, 2040, and 2050.

Increase local commercial food sourcing

- Increase by 10%, 25%, 50% or more restaurants, farm stands, or market sourcing from local producers by 2030, 2040, and 2050



CECAP Awards

- **EPA:** Leadership in Energy Efficiency(2020)
- **UN Foundation of Dallas**: Global Leadership Award for SDG 11, Sustainable Cities & Communities (2020)
- **American Planning Association**: Award for Sustainability, by the APA - Sustainable Communities Division (2021)
- **NCTCOG**: Celebrating Leadership in Development Excellence (CLIDE) Award for Equity & Inclusion (2021)
- **CDP "A-List" Award:** Global Leadership in Climate Action (2021, 2022)
- **AIA Dallas Community Honor:** Sustainability Commendation for Environmental Leadership (2021)
- **APA:** National Award for Environmental Leadership (2022)
- **Brookings Institute**: Top City Climate Plan for Implement ability (2022)

Select Climate Legislation/Bills

State Law

- **HB17 (signed 2021)**: Prohibits municipalities from restricting the use of any energy type or source, such as natural gas.

State Bills

- **H.B. 2211 (Landgraf) – Greenhouse Gasses**: would disallow cities from creating an ordinance that directly regulates greenhouse gas emissions. **Companion: S.B. 784 (Birdwell)**
- **H.B. 2374 (Landgraf) – Restricting a Fuel Source:** would disallow cities from creating an ordinance or regulation that limits access to an energy source. A city may not adopt an ordinance or regulation that restricts the use, sale, or lease of an engine based on a fuel source. **Companion: S.B. 1017 (Birdwell)**
- **S.B. 1114 (Hancock) – Restricting a Fuel Source**: would disallow cities from passing an ordinance or regulation that restricts the use of a fuel source to aid in the reduction of greenhouse gases or conservation of natural resources. This includes entering into a contract that would directly or indirectly the use or sale of a product otherwise permitted by law.

Questions??

Comprehensive Environmental and Climate Action Plan (CECAP): Climate Mitigation and Adaptation

City of Dallas

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How Algorithm Assisted Decision Making Is Influencing Environmental Law and Climate Adaptation

ELPAR Presentation

March 31, 2023

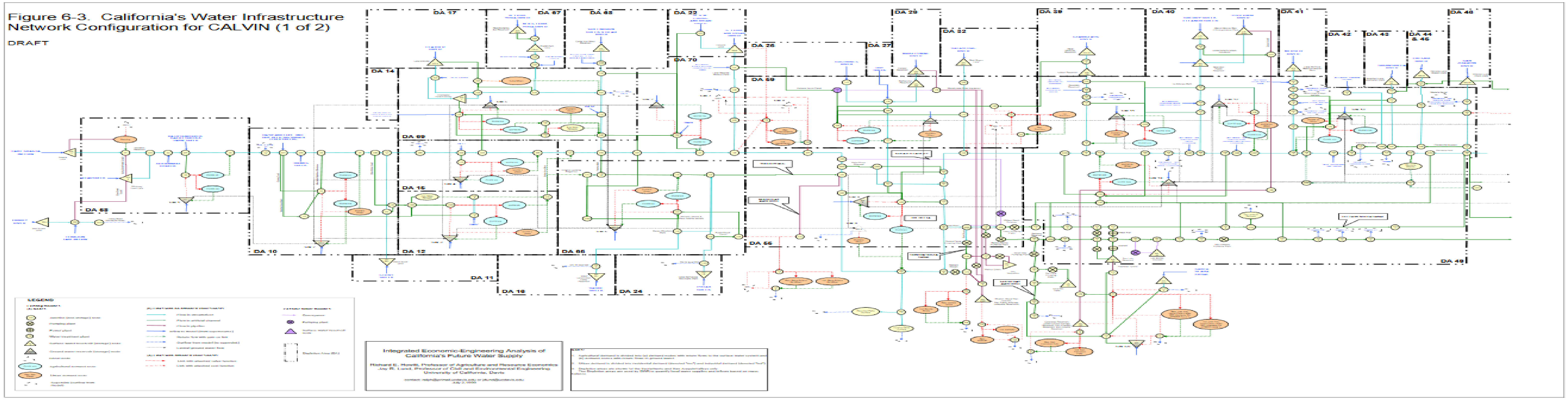
Sonya Ziaja, JD, MSc, PhD

Assistant Professor, University of Baltimore

Takeaway First:

Algorithmic tools are new fora for environmental decision making.

Traditional and New Places of Decision Making



Why should you care?

1. **Climate adaptation depends on these tools.**

2. **Algorithmic tools embed value laden assumptions and biases, which influence climate adaptation and law.**

3. **The “rules” of this new kind of forum necessarily impede equity and democratic participation (***w/out deliberate counter measures***).**

Forum Argument: Algorithmic tools are new fora for environmental decision making

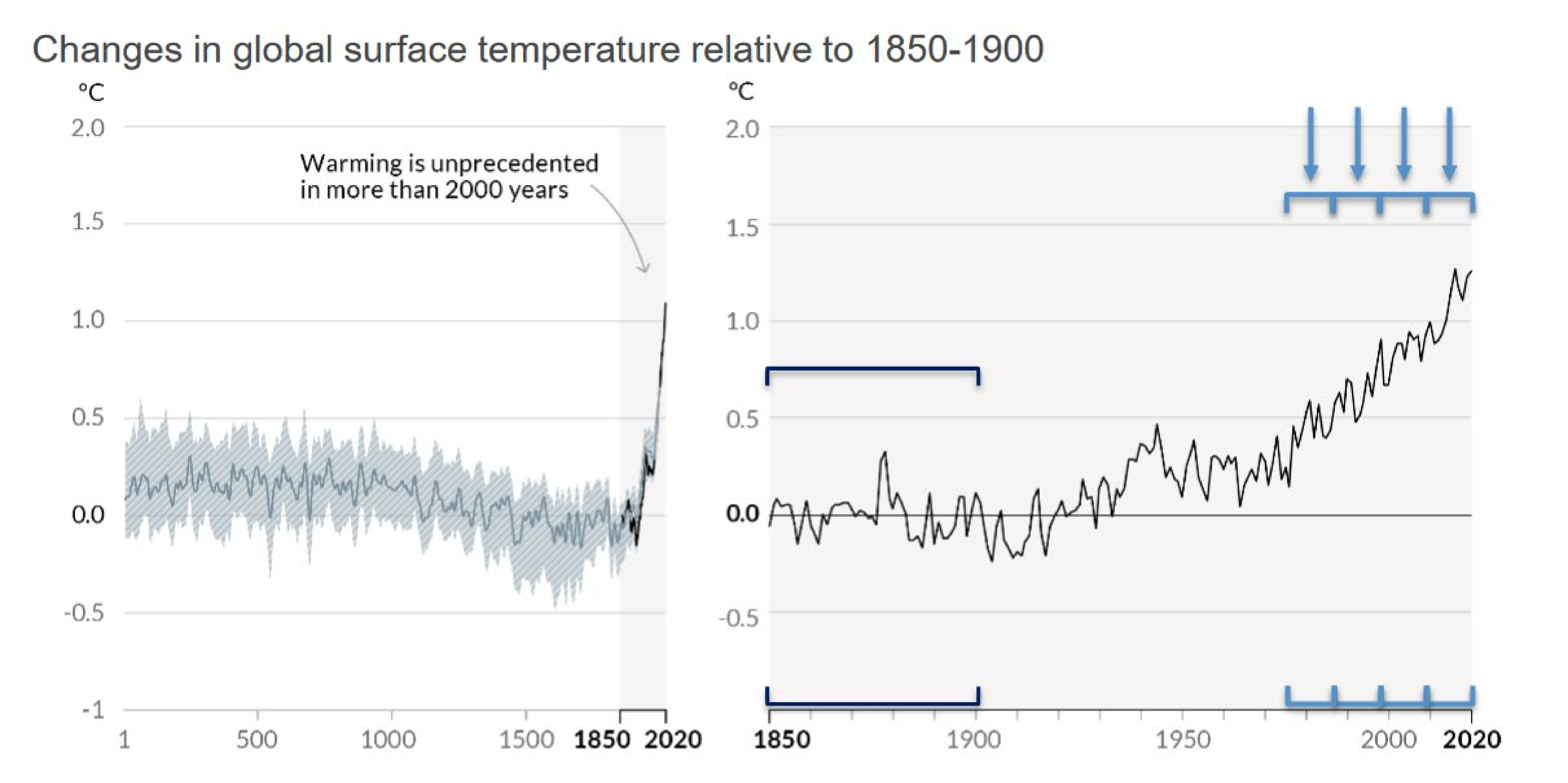
- In practice, what these tools are doing what legislatures, courts, and deliberative bodies do.

- Pol Sci: *Politics is "who gets what, when and how" (Lasswell). Also, who decides and how we decide such things (Schlager and Blomquist)*.

- Allocating resources according to internal rules (who gets what water when and how).

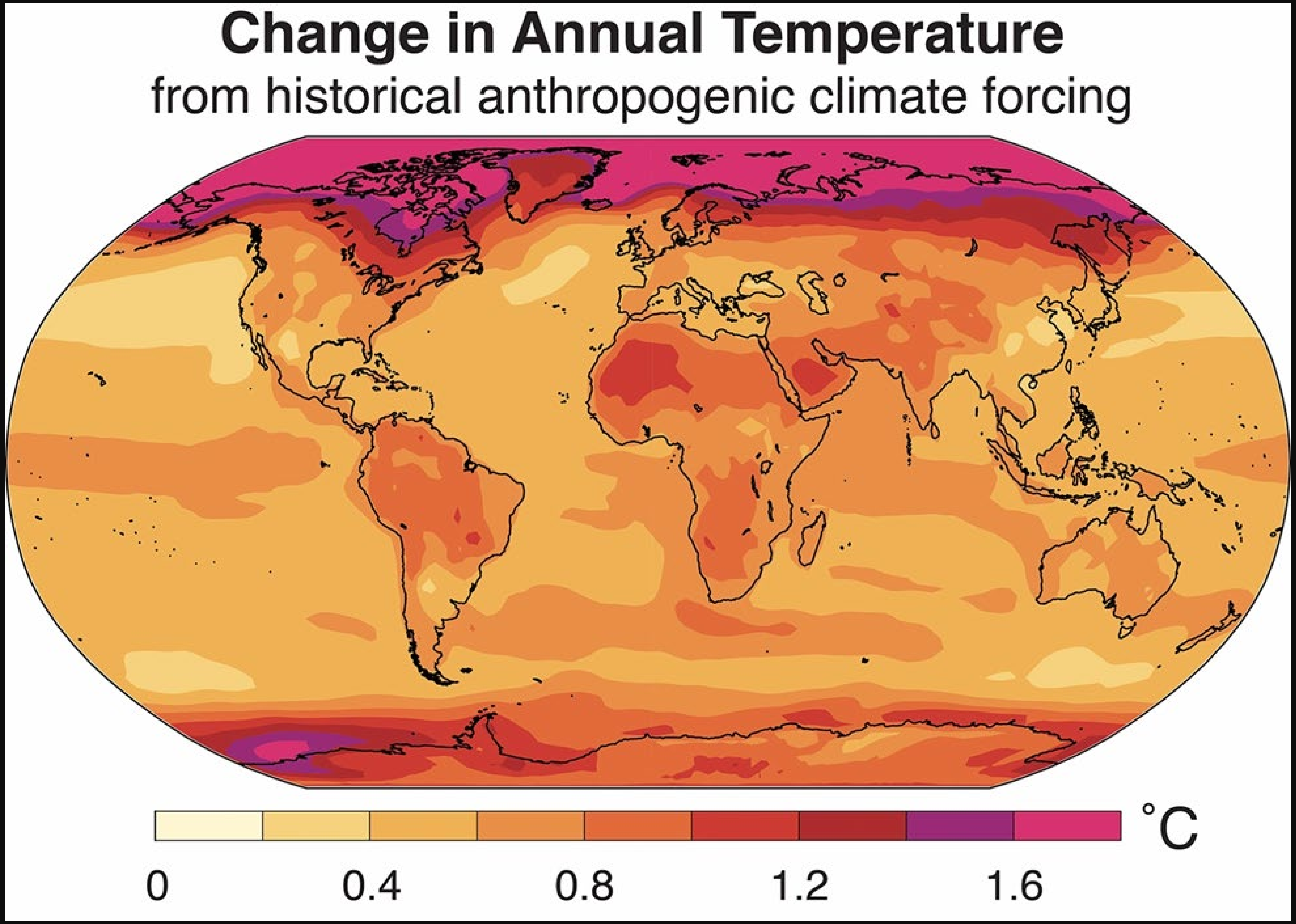
Why should you care?
1. Climate adaptation depends on these tools.

- Climatic *patterns have diverged* from the historical envelope. We cannot rely on the past as a predictor of the future *(nonstationarity).*



(IPCC Sixth Assessment Report 2021)

Why should you care?
1. Climate adaptation depends on these tools.

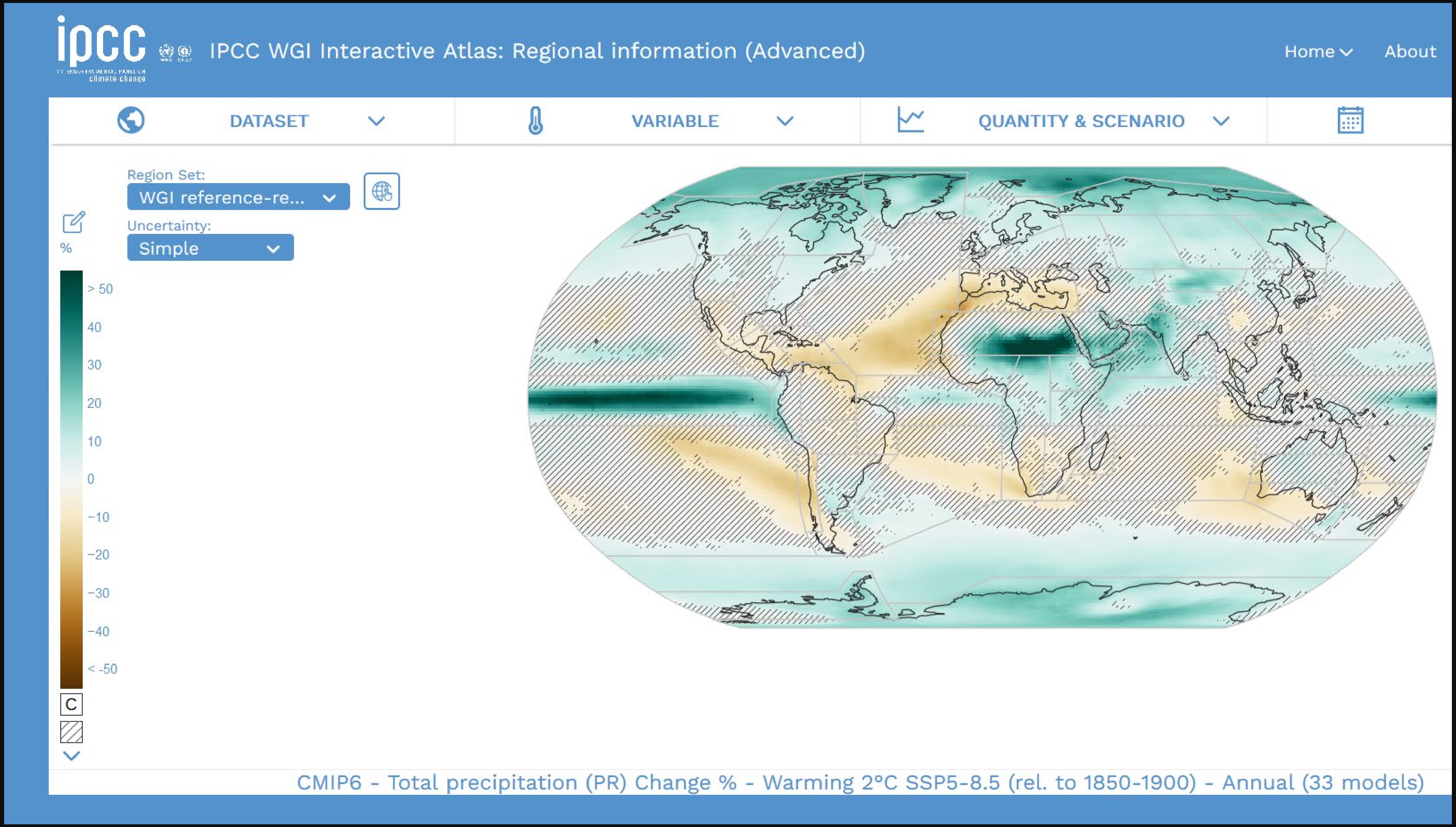


(Diffinbaugh and Burke 2019)

- Changes in temperature are not evenly distributed.

Why should you care?

1. Climate adaptation depends on these tools.



- Changes in temperature are not evenly distributed.
- Changes in precipitation patterns are also variable globally, and locally.

(IPCC Sixth Assessment Report, Interactive Atlas, https://interactive-atlas.ipcc.ch/)

Why should you care?

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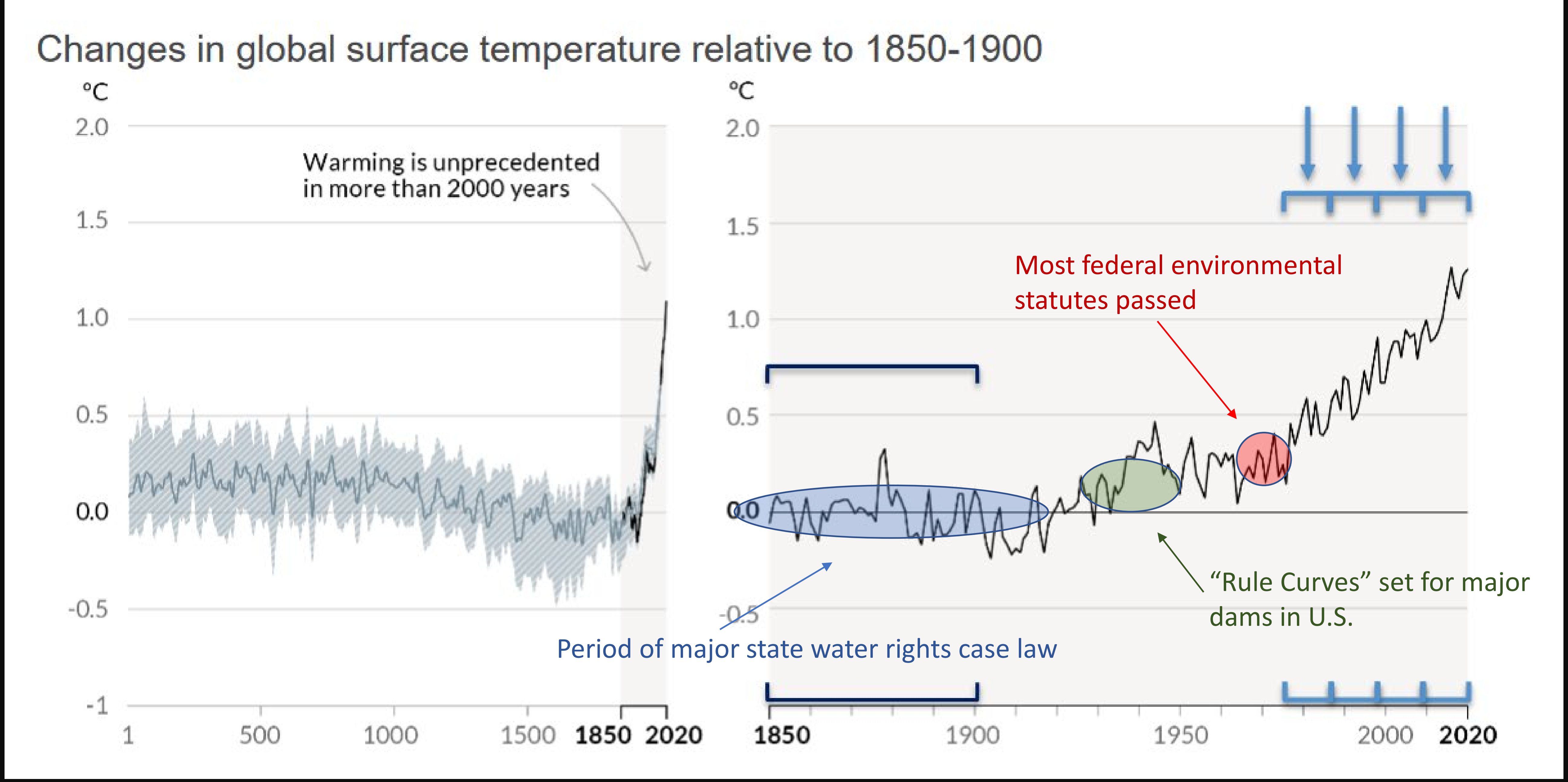

(IPCC Sixth Assessment Report 2021)

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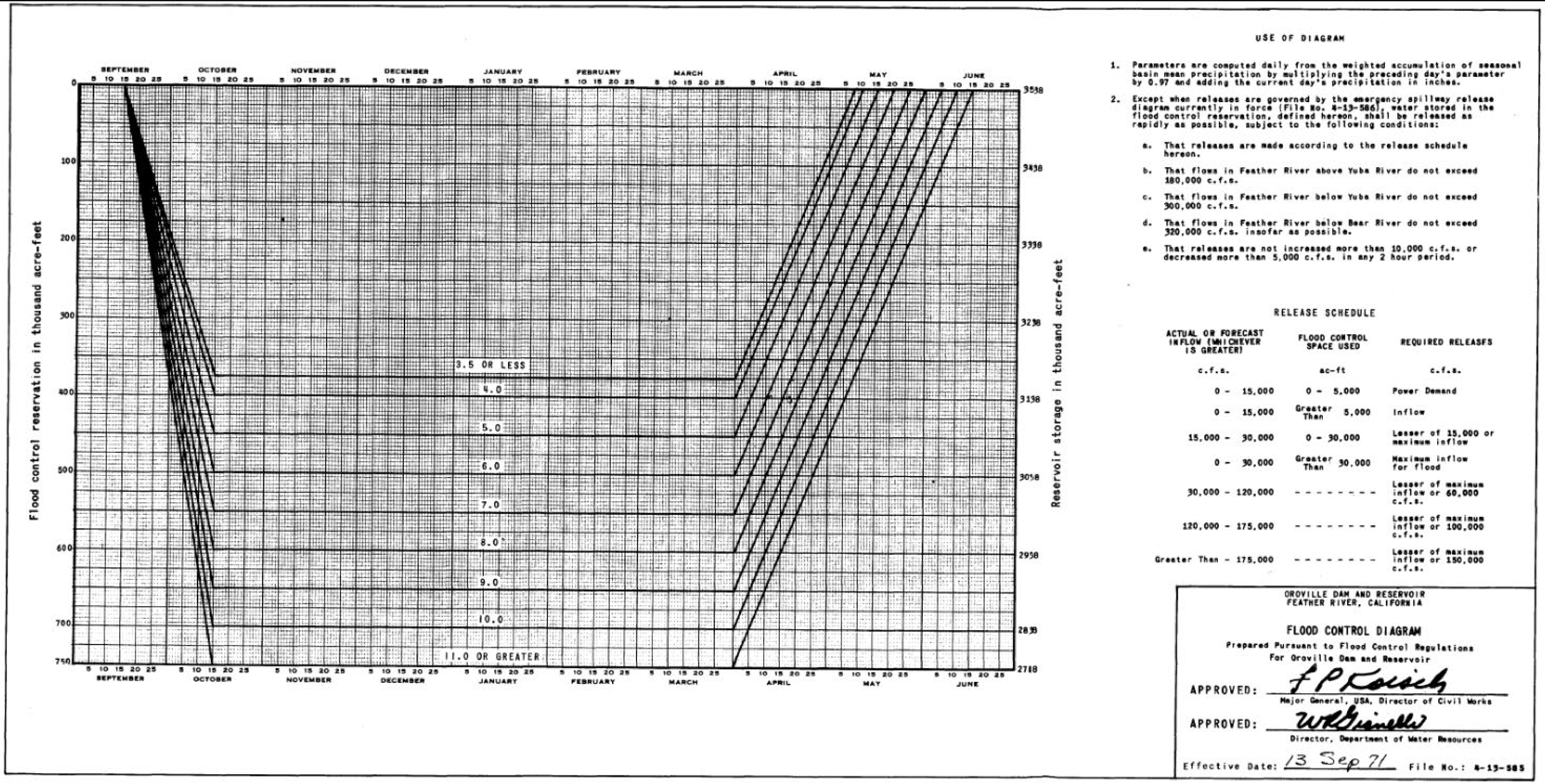


Source: USACE 1970

Why should you care?
1. Climate adaptation depends on these tools.

Climatic patterns have diverged from the historical envelope. We cannot rely on the past as a predictor of the future *(nonstationarity).*

Algo Tools

Because we cannot rely on the past, we need scenario development and ways to interpret those scenarios.

Algorithmic tools are how we develop scenarios.

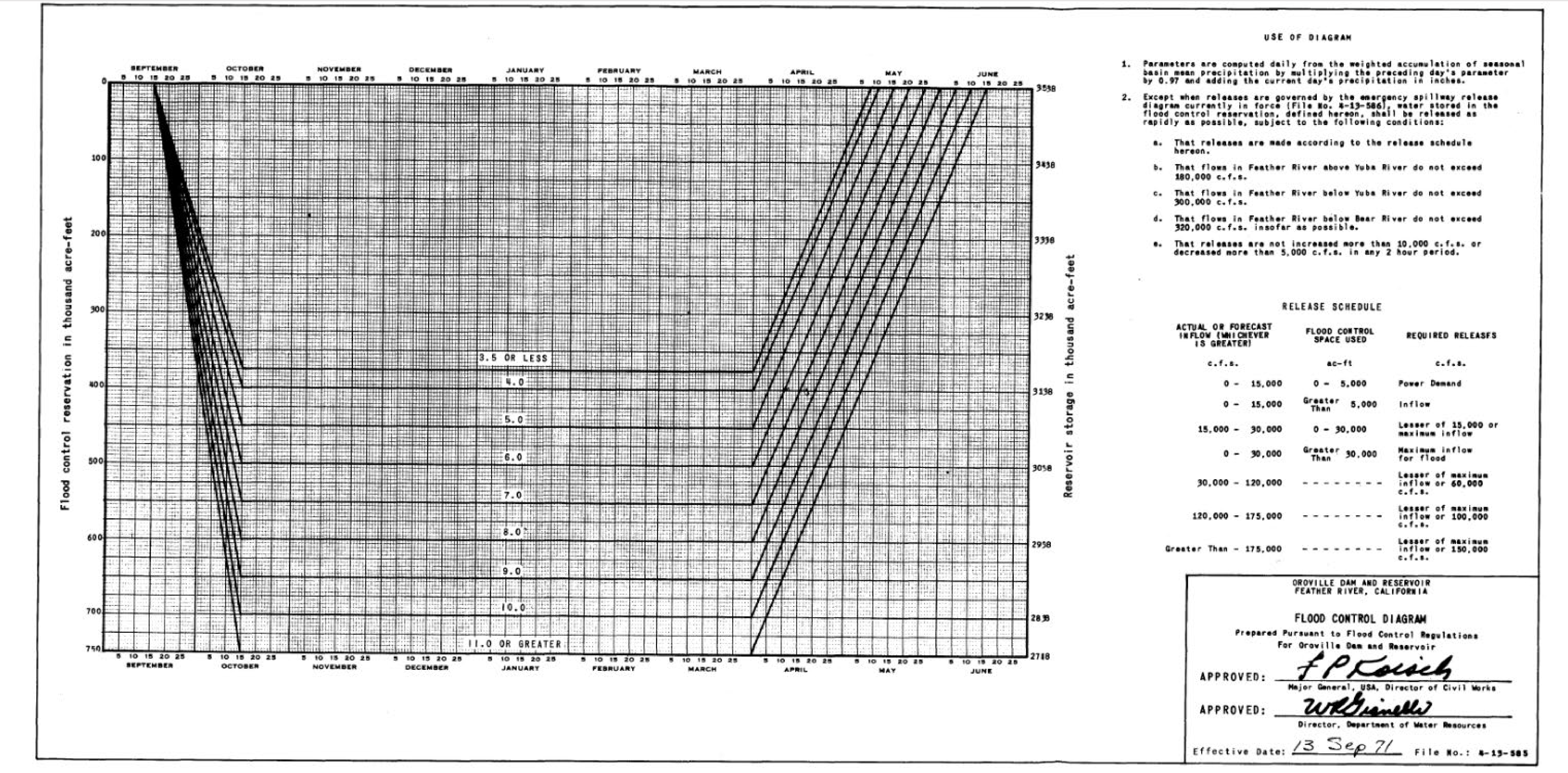
Why should you care?

2. Algorithmic tools embed value laden assumptions and biases which influence climate adaptation and law.

- How? 3 Pathways:
  1. Uncertainty
     - "All models are wrong, but some are useful."
     - Process of simplification, choices need to be made, those choices will drive the outcome of the model/ making those choices is <u>value laden</u>
  2. Transparency (or lack thereof)
     - Explanations may be insufficient
  3. Characteristics of the network and development process
     - Who is involved in development, in what role, and when

Why should you care?

2. Algorithmic tools embed value laden assumptions and biases which influence climate adaptation and law. *(Uncertainty, Transparency, and Process)*



USE OF DIAGRAM

1. Parameters are computed daily from the weighted accumulation of seasonal basin mean precipitation by multiplying the preceding day's parameter by 0.97 and adding the current day's precipitation in inches.

2. Except when releases are governed by the emergency spillway release diagram currently in force (File No. 4-13-586), water stored in the flood control reservation, defined hereon, shall be released as rapidly as possible, subject to the following conditions:

   a. That releases are made according to the release schedule hereon.

   b. That flows in Feather River above Yuba River do not exceed 180,000 c.f.s.

   c. That flows in Feather River below Yuba River do not exceed 300,000 c.f.s.

   d. That flows in Feather River below Bear River do not exceed 320,000 c.f.s. insofar as possible.

   e. That releases are not increased more than 10,000 c.f.s. or decreased more than 5,000 c.f.s. in any 2 hour period.

RELEASE SCHEDULE

ACTUAL OR FORECAST INFLOW (WHICHEVER IS GREATER)	FLOOD CONTROL SPACE USED	REQUIRED RELEASFS
c.f.s.	ac-ft	c.f.s.
0 - 15,000	0 - 5,000	Power Demand
0 - 15,000	Greater Than 5,000	Inflow
15,000 - 30,000	0 - 30,000	Lesser of 15,000 or maximum inflow
0 - 30,000	Greater Than 30,000	Maximum inflow for flood
30,000 - 120,000	- - - - - - - -	Lesser of maximum inflow or 60,000 c.f.s.
120,000 - 175,000	- - - - - - - -	Lesser of maximum inflow or 100,000 c.f.s.
Greater Than - 175,000	- - - - - - - -	Lesser of maximum inflow or 150,000 c.f.s.

OROVILLE DAM AND RESERVOIR
FEATHER RIVER, CALIFORNIA

FLOOD CONTROL DIAGRAM

Prepared Pursuant to Flood Control Regulations
For Oroville Dam and Reservoir

APPROVED: F P Koisch
Major General, USA, Director of Civil Works

APPROVED: W R Gianelli
Director, Department of Water Resources

Effective Date: 13 Sep 71 File No.: 4-13-585

<u>Why should you care?</u>

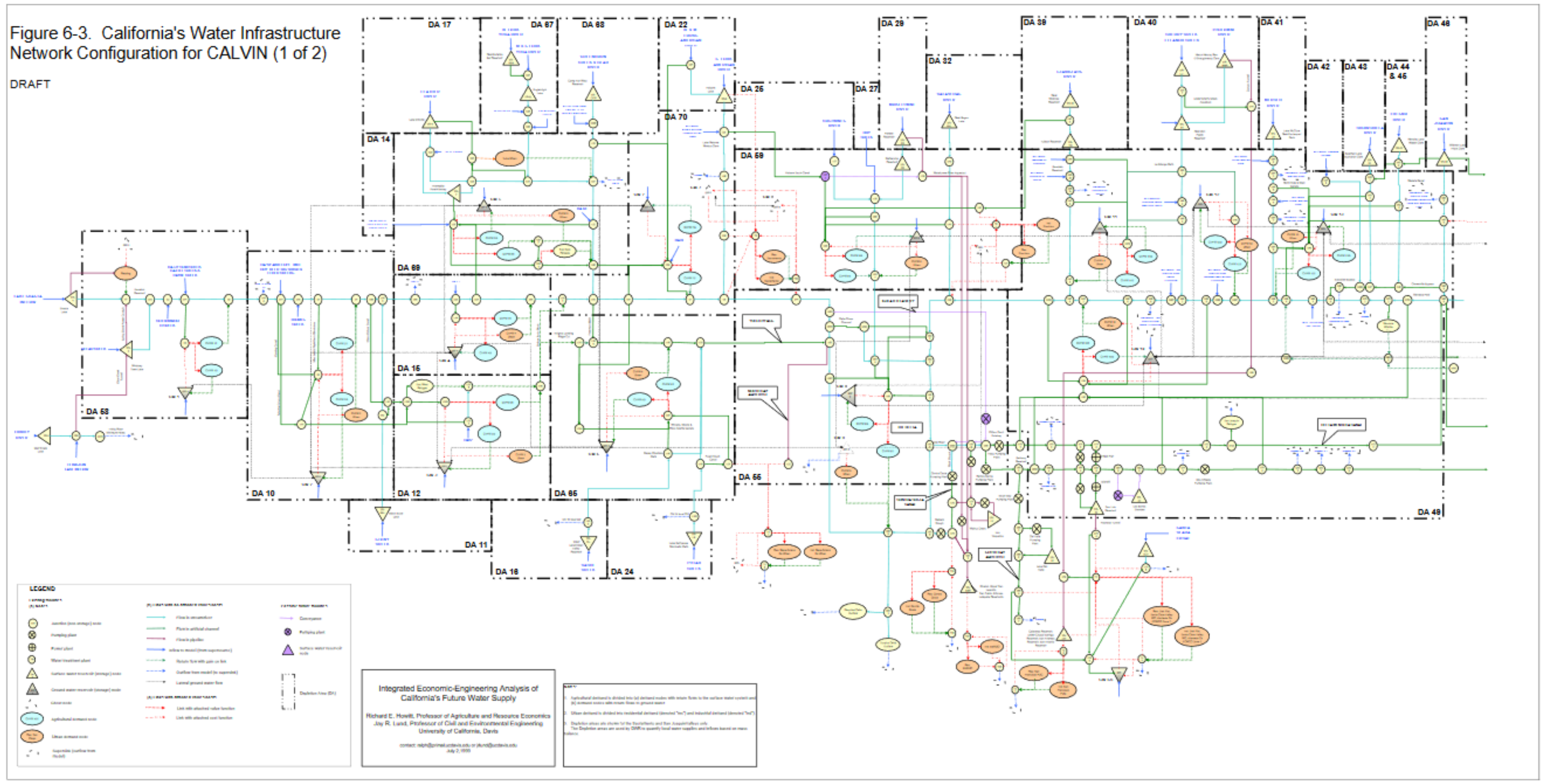
3. **The "rules" of this new kind of forum necessarily impede equity and democratic participation-** w/out deliberate counter measures

Allocation, <u>BUT with deliberation</u>

- Publicly known and available rules
- Informed network of actors
- In a language, albeit with jargon and at times behind closed doors, that is intelligible.

Why should you care?

3. The “rules” of this new kind of forum necessarily impede equity and democratic participation- w/out deliberate counter measures



Allocation, but with <u>no public deliberation</u>

Simplification requires value laden assumptions to be made

Difficult to access and understand

Difficult to review

Why should you care?

3. The “rules” of this new kind of forum necessarily impede equity and democratic participation- w/out deliberate counter measures

- Energy, natural resource, and environmental decisions are inherently technical (Already difficult to understand and difficult to access)- Reliance on algorithmic tools makes these decisions even more opaque and difficult to access.

- Model functioning and development necessarily embeds biases and value laden assumptions

- Networks that develop these tools are highly educated technocrats

Why should you care?

- **Climate adaptation depends on these tools**
- **Algorithmic tools embed value laden assumptions and biases which influence climate adaptation and law**
- **The "rules" of this new kind of forum necessarily impede equity and democratic participation-** w/out deliberate counter measures

Framework for considering equity in algorithmic tools

	Model Itself	Design Process
Uncertainty	How is governance and conflict represented? To what extent do the model's mechanisms for assigning weighted values and choosing optimal solutions reflect existing governance? What are the kinds of uncertainty in the system being modeled that simplification may obscure?	How is uncertainty communicated and to whom? Who is involved in determining sources of uncertainty?
Transparency	Is the logic of the model explicable? What aspects, if any, of the model are "black box" and unknowable? Are the inputs and parameters open to verification from outside sources?	Are participants in the design and implementation known?
Stakeholder Collaboration	Is stakeholder collaboration advisory or determinative? Is stakeholder knowledge incorporated into the model?	Who determines which stakeholders are relevant? With what parameters? Can stakeholders themselves expand who participates? To what extent do stakeholders determine processes for collaboration? How are disagreements among stakeholders and designers resolved?

Framework for considering equity in algorithmic tools

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Stakeholder Collaboration	Is stakeholder collaboration advisory or determinative? Is stakeholder knowledge incorporated into the model?	Who determines which stakeholders are relevant? With what parameters? Can stakeholders themselves expand who participates? To what extent do stakeholders determine processes for collaboration? How are disagreements among stakeholders and designers resolved?

Is equity (substantive and procedural) included in the network for producing algorithmic tools?

Summary of Argument

- Algorithmic tools are new fora for environmental decision making.
- You should care because…
  - Climate adaptation depends on these tools
  - The tools embed value laden assumptions and biases which influence climate adaptation and law, through uncertainty, issues with transparency, and characteristics of their development networks
  - The “rules” of the new forum impede equity and democratic participation.
- It may be possible to make equity considerations more apparent through use of a framework, which considers characteristics of the tool and its development.

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Do ESG Mutual Funds Deliver on Their Promises?

Quinn Curtis, Jill E. Fisch & Adriana Z. Robertson

Environmental Law & Policy Annual Review
Washington, DC Conference
March 31, 2023

Background

The Rise of ESG Investing

Concerns about ESG Funds – the debate over the DOL policy and the SEC's proposed rulemakings:

- What are investors *getting* for their ESG dollars?
- What are investors *giving up* when they invest in ESG funds?

Politicization of ESG investing

- Greenwashing challenges from the left
- Anti-ESG efforts from the right
- Public pension funds
- State anti-ESG legislation

Regulatory Developments

Since the publication of our paper, regulatory and media focus on ESG has intensified

SEC Regulatory Initiatives

- March 2022 - Proposed rule on climate risk disclosure
- May 2022 – Proposal to extend the Names Rule of the Investment Company Act to ESG investing
- May 2022 – Proposal to enhance disclosures by Investment Advisers (ESG fund buckets & disclosure of weighted average carbon emissions)

DOL Regulatory Initiatives

- Most recently, Nov. 2022 adoption of rule to remove barriers to ESG investing

Recent congressional votes to void the DOL's ESG rule

If Biden vetoes the resolution, it will be his first veto

What we did

We examined whether ESG funds differ from non-ESG funds along four dimensions:

- Portfolio composition
- Voting behavior
- Costs
- Performance

We found:

- significant differences in portfolio composition and voting behavior
- no evidence that ESG funds cost more or underperform non-ESG funds

Caveats

What is ESG?

- Reasonable minds can disagree
- Climate change, human capital management, private prisons
- Tesla?
- We do not adopt our own definition

What is an ESG strategy?

- Screening and exclusion
- Invest in the "better" companies in an industry or sector
- Impact investing
- Tilt strategies
- Potential breadth – other values funds, anti-ESG funds

Criticism of ESG ratings

- We are agnostic here and use four different ratings providers
- We do not purport to analyze how much ESG is "enough"

Caveats

Our analysis focused on a specific moment in time:

- Substantial recent growth in number and size of ESG funds
- Funds continue to refine their investment strategies and disclosures
- Increasing fund variety on both the left and the right
- Some non-ESG funds consider ESG issues
- Performance numbers may also be a function of general market conditions
  - Ukraine war
  - Tech collapse

Empirical Analysis

Sample of Funds

ESG Names

- Does the fund name suggest that it is ESG focused? (ex., sustainable; responsible; ESG; green; etc)

Morningstar-identified

- Does Morningstar identify it as an ESG fund?

Separately, we study funds Morningstar identifies as ESG Consideration funds

- "Consider" ESG in their decisionmaking

Data

Holdings and Performance Data $\Rightarrow$ CRSP ESG Ratings from four different providers:

- Sustainalytics
- S&P
- ISS
- TruValue Labs

Sample Period: 2018-2019

What are Investors Getting?

The SEC's primary concern is that investors are being misled

We ask: Is there evidence that ESG funds are systematically failing to differentiate themselves with respect to

- Their portfolio tilt?
- Their voting behavior?

Do ESG Funds have "more ESG" Portfolios?

We construct ESG tilt of each fund $\times$ quarter

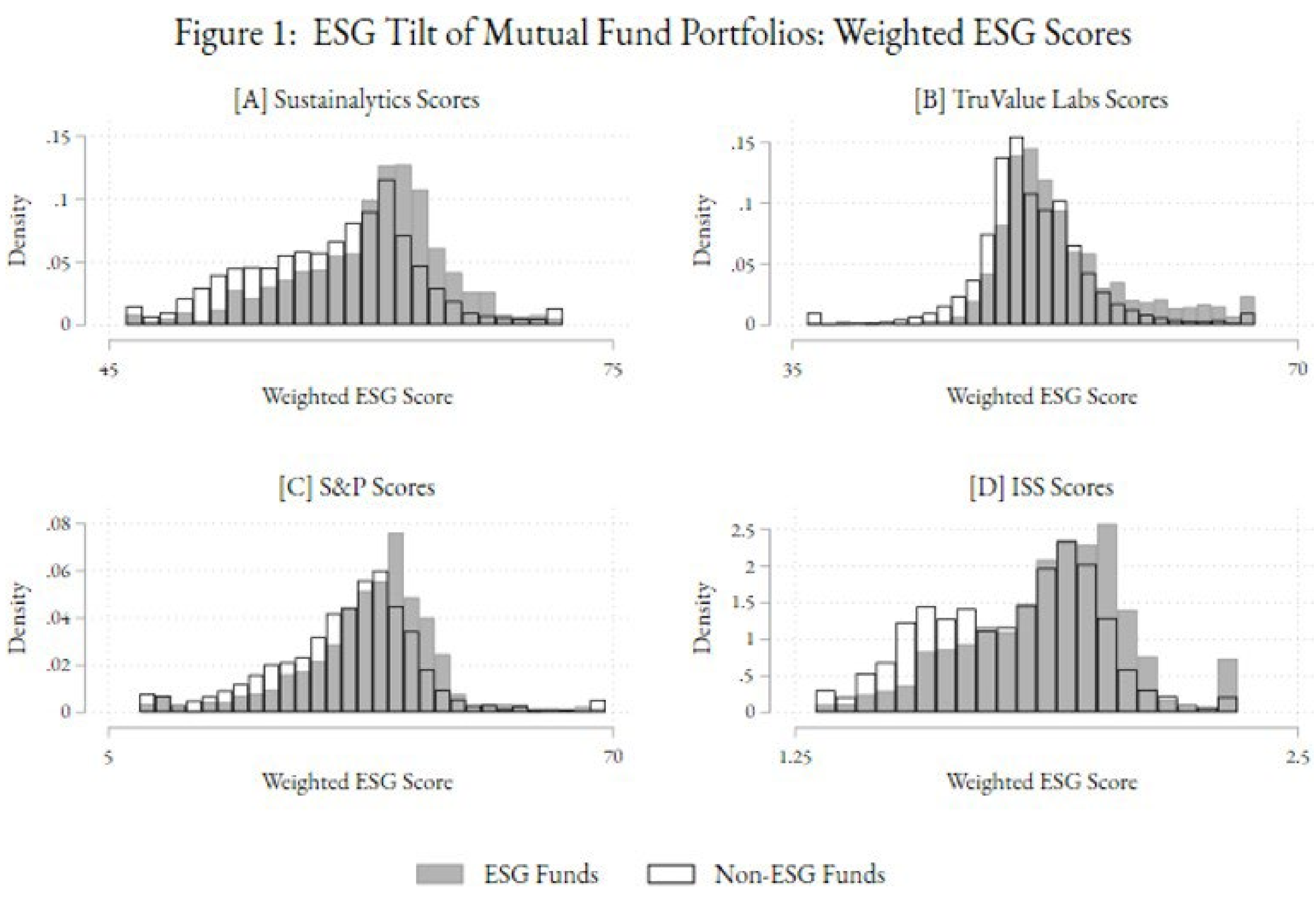
$$Tilt_{(j,t,k)} = \Sigma_i \, w_{i,j,t} \times r_{i,t,k}$$

Where

- $w_{i,j,t}$ is the weight of security i in fund j's portfolio in quarter t
- $r_{i,t,k}$ is the ESG rating of security i in period t, as rated by entity k

We also construct percentile scores using these ratings

For the Most Part, Yes



On Average, Yes

Table 2: ESG Portfolio Tilts- ESG/Non-ESG Funds

Panel A: ESG Tilt Measured by Weighted ESG Scores								
	Sustainalytics Scores		TruValue Labs Scores		S&P Scores		ISS Scores	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
ESG Name	1.775***		2.223***		3.048***		0.101***	
	(7.01)		(7.03)		(5.38)		(7.96)	
Morningstar		1.212***		1.539***		2.515***		0.051***
		(3.97)		(6.56)		(4.22)		(4.61)
Objective Code x Quarter FE	YES	YES	YES	YES	YES	YES	YES	YES
N	46,432	46,432	50,658	50,658	41,778	41,778	48,304	48,304
adj. R-sq	0.071	0.071	-0.002	-0.002	-0.002	-0.002	0.046	0.046
Number of ESG Funds	174	200	189	218	164	186	182	211

Percentiles

Voting Analysis

Do ESG funds vote differently?

- Look at propensity to oppose management
- Try to isolate ESG funds vs ESG families
Shareholder proposals
- Essentially all ESG relevant

Environmental shareholder proposals and "E" funds:

- Easier to identify

Uncontested director elections:

- General propensity to oppose management

Voting - Results

Table 5: Likelihood of Voting Against Management Recommendation (LPM)- ESG/Non-ESG Funds						
	Shareholder Props.		Unopposed Director Elections	Shareholder Props.		Unopposed Director Elections
	(1)	(2)	(3)	(4)	(5)	(6)
ESG Fund Indicator	0.126*** (4.16)		0.020*** (3.29)	0.117*** (5.55)		0.019*** (4.71)
Enviro Fund Indicator		-0.036 (-1.02)			0.063 (1.25)	
Enviro Issue Indicator		-0.064*** (-18.63)			-0.064*** (-17.50)	
Enviro Fund x Enviro Issue		0.126** (3.07)			0.137* (2.51)	
ESG Family Indicator	0.271*** (7.95)	0.387*** (17.75)	0.238*** (6.16)			
Constant	0.460	0.469	0.060	0.463***	0.471***	0.061***
Firm x Year FE	**Yes**	**Yes**	**Yes**	No	No	No
Fund Fam. X Firm X Yr. FE	No	No	No	**Yes**	**Yes**	**Yes**
Observations	788,913	788913	14,438,612	788,913	788913	14,438,612
R-squared	0.283	0.282	0.205	0.653	0.652	0.515

What are Investors Giving Up?

The DOL's primary concern is that ESG funds are sacrificing pecuniary performance for non-pecuniary goals

We ask: Is there evidence that ESG funds are systematically underperforming with respect to

- Their expenses?
- Their performance?

Higher Fees?

Table 6: Expense Ratios - ESG/Non-ESG Funds

	(1)	(2)	(3)
ESG Name	-0.00049		
	(-1.47)		
Morningstar		0.00017	
		(0.70)	
Morningstar Consideration			0.00079***
			(4.31)
Observations	52,592	52,592	52,592
Adjusted R-squared	0.340	0.340	0.341
Number of ESG Funds	178	218	249

All models include: manager, fund, and class size controls; objective x year fixed effects and index fund fixed effects

Note: We are not showing (or claiming) that ESG funds are as cheap as the ultra-low-cost index funds

Worse (Pecuniary) Performance?

Table 7: Returns and Sharpe Ratios - ESG/Non-ESG Funds

	(1)	(2)	(3)	(4)	(5)	(6)
ESG Name	0.00214*			0.04917*		
	(2.62)			(2.80)		
Morningstar		0.00090			0.01647	
		(1.86)			(1.62)	
Morningstar Consideration			0.00127**			0.02667**
			(3.43)			(3.06)
Observations	721305	721305	721305	721186	721186	721186
Adjusted R-squared	0.651	0.651	0.651	0.780	0.780	0.780
Number of ESG Funds	202	234	260	201	233	259

All models include: manager, fund, and class size controls; objective x month fixed effects and index fund fixed effects

Regulatory Implications

What does this mean for the SEC?

The moral panic about ESG funds may be overblown

- At the portfolio level, ESG ratings may not be so problematic
- ESG funds **do** tend to have portfolios with more ESG tilt
- ESG funds **do** seem to vote more independently

Investors may not understand exactly how the ESG evaluation is done, or exactly how the fund is run, but that's true of all mutual fund strategies!

Bottom line: Our analysis does not demonstrate a need to treat ESG funds differently from other mutual funds

Current SEC rule proposals that introduce distinctive compliance obligations on ESG funds may limit innovation

What does this mean for the DOL?

No obvious reason to discourage ESG considerations by pension fund trustees

No obvious reason to discourage ESG funds in participant-directed retirement plan menus

No obvious reason to *require* the consideration of ESG factors by fiduciaries

The End

Tilt - Regression (Percentiles)

Table 2: ESG Portfolio Tilts- ESG/Non-ESG Funds

Panel B: ESG Tilt Measured by ESG Percentile

	Sustainalytics Scores		TruValue Labs Scores		S&P Scores		ISS Scores	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
ESG Name	12.377***		14.899***		11.873***		13.273***	
	(7.90)		(8.23)		(6.60)		(9.01)	
Morningstar		9.018***		12.355***		9.105***		7.498***
		(5.41)		(8.49)		(4.86)		(4.88)
Objective Code x Quarter FE	YES	YES	YES	YES	YES	YES	YES	YES
N	46,432	46,432	50,658	50,658	41,778	41,778	48,304	48,304
adj. R-sq	0.381	0.380	0.247	0.246	0.263	0.261	0.402	0.399
Number of ESG Funds	174	200	189	218	164	186	182	211

Back

Arnold & Porter
Innovative. Integrated. Industry-Focused.

Department of Labor Regulation of ESG Investing

Kathryn Geoffroy

March 31, 2023

Duty of Prudence

- Retirement plans such as 401(k) plans and pension plans are generally subject to the Employee Retirement Income Security Act of 1974 ("ERISA")
- As mentioned by the paper, fiduciaries of ERISA plans are subject to certain fiduciary duties, including the duty of prudence and the duty of loyalty
  - The duty of prudence is the duty to act "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims"
- Fiduciaries have an ongoing duty to select and maintain investment options for the plan that are prudent
- Fiduciary duty breaches related to selection of plan investment are a focus of many class-action lawsuits which are complex and expensive to defend

2020 Final Regulations

- Prior to 2020, the Department of Labor released guidance on ESG-type issues from time to time
- In October 2020, the Department of Labor released final regulations
  - ERISA plan fiduciaries may not subordinate return or increase risks to promote non-pecuniary objectives
  - Required additional documentation if plan fiduciaries considered nonpecuniary factors as “tie-breakers” between investment alternatives that were indistinguishable based on pecuniary factors alone
  - Prohibited plan fiduciaries from selecting ESG-focused investments as “qualified default investment alternatives” for an ERISA plan if the investment objectives or goals or principal investment strategies include, consider, or indicate the use of one or more non-pecuniary factors

Proposed 2021 Regulations and Final 2022 Regulations

- After announcing the non-enforcement of the 2020 regulations, on October 14, 2021, the Department of Labor proposed new regulations relating to investment by ERISA plans in ESG-focused funds
- Final regulations were released on December 1, 2022
- Key changes from 2020 final regulations:
  - A prudent fiduciary may consider *any factor* material to the risk-return analysis when selecting investments
  - Allow fiduciaries to consider collateral benefits of investments in the case of a "tie-breaker"
  - Generally eliminate documentation requirements under the 2020 ESG regulations for considering nonpecuniary factors, other than for designated investment alternatives selected for the collateral benefits they create
- The new regulations reiterate long-standing Department of Labor guidance that a fiduciary may not sacrifice investment returns or take additional investment risk to promote benefits or goals unrelated to the interests of the participants and beneficiaries

ESG Backlash

- Due to political controversy, this is an area that is subject to change
- Several states have passed anti-ESG laws or have had governors announce that no state funds are invested using ESG principles
- Congress passed legislation which sought to overturn the Department of Labor’s 2022 final rule regarding ESG investments, which President Biden used his first veto of his term to reject.
- A coalition of 25 states sued the Department of Labor seeking to stop the new 2022 final regulations from taking effect.

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