No. 23-11097

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

STATE OF UTAH, ET AL,
Plaintiffs-Appellants,

v.

JULIE A. SU, ET AL,
Defendants-Appellees.

On Appeal from the United States District Court
for the Northern District of Texas
No. 2:23-cv-016; Hon. Matthew J. Kacsmaryk

BRIEF OF THE NATIONAL FEDERATION OF INDEPENDENT BUSINESS SMALL BUSINESS LEGAL CENTER, INC. AND TEXAS PUBLIC POLICY FOUNDATION AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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Pursuant to Fifth Circuit Rule 29.2, *amici curiae* state that, in addition to the interested persons identified in the parties' briefs, no person other than *amici curiae* The National Federation of Independent Business Small Business Legal Center, Inc. and Texas Public Policy Foundation have an interest in this *amicus* brief.

/s/Christian Townsend
CHRISTIAN TOWNSEND

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INTEREST OF *AMICI CURIAE*[1]

The National Federation of Independent Business Small Business Legal Center, Inc. (NFIB Legal Center) is a nonprofit, public interest law firm established to provide legal resources and be the voice for small businesses in the nation's courts through representation on issues of public interest affecting small businesses. It is an affiliate of the National Federation of Independent Business, Inc. (NFIB), which is the nation's leading small business association. NFIB's mission is to promote and protect the right of its members to own, operate, and grow their businesses. NFIB represents, in Washington, D.C., and all 50 state capitals, the interests of its members.

Amicus NFIB Legal Center files here because the Department of Labor's new fiduciary rule is stripped of requirements designed to protect retirement plan sponsors, many of whom are small businesses. It will force small businesses to engage in their own oversight of fiduciaries that will prove both costly and time-consuming.

The Texas Public Policy Foundation (TPPF) is a non-profit, non-partisan research organization dedicated to promoting liberty, personal

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[1] Pursuant to Federal Rule of Appellate Procedure 29(a), counsel for *amici* states that all parties have consented to the filing of this brief. Counsel further affirms that no counsel for a party authored this brief in whole or in part, and no person other than *amici* and their counsel made a monetary contribution to its preparation or submission.

responsibility, and free enterprise through academically sound research and outreach.

Since its inception in 1989, the Foundation has emphasized the importance of limited government, free market competition, private property rights, and freedom from regulation. In accordance with its central mission, the Foundation has hosted policy discussions, authored research, presented legislative testimony, and drafted model ordinances to reduce the burden of government on Texans. Historically, the Foundation has worked through its Life:Powered project to advocate for energy policies that promote economic freedom and advance the human condition. As a part of this research TPPF has warned about the dangers of emphasizing ESG criteria in investment decisions and have argued that return on investment should be the sole criteria for investment decisions.

INTRODUCTION AND SUMMARY OF ARGUMENT

The Department of Labor ("DOL") promulgated a rule at 87 *Fed. Reg.* 73822 (codified at 29 CFR § 2550) ("2022 Rule") that revised the duties of fiduciaries for employee benefit plans under the Employment Retirement Income Security Act of 1974 ("ERISA"). ERISA requires, in relevant part, "the disclosure and reporting to participants . . . of financial and other information . . . by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans[.]" 29 U.S.C. § 1001(b). Chief among these duties is the obligation to act for the "exclusive purpose of: (i) providing benefits to participants and their beneficiaries; and (ii) defraying reasonable expenses of administering the plan[.]" 29 U.S.C. § 1104(a)(1).

The word "benefits" must be read narrowly. *See United States v. Am. Trucking Ass'ns*, 310 U.S. 534, 544 (1940) ("A few words of general connotation appearing in the text of statutes should not be given a wide meaning, contrary to a settled policy, excepting as a different purpose is plainly shown."(internal quotations omitted)). The U.S. Supreme Court, in *Fifth Third Bancorp v. Dudenhoeffer* confirmed this, holding that the "benefits" referenced in § 1104(a)(1) "must be understood to refer to the sort of *financial* benefits (such as retirement income) that trustees who manage investments typically seek to secure for the trust's beneficiaries." 573 U.S. 409, 420–21 (2014).

Before the 2022 Rule, DOL seemed to accept this reading of the statute, severely limiting fiduciaries' ability to use non-financial considerations in choosing investments. The 2020 Rule, 29 CFR § 2550, was clear that fiduciaries can only use collateral factors like Environmental, Social, and Governance ("ESG") to make investment decisions as a tiebreaker, when they are "unable to distinguish" investments "on the basis of pecuniary factors alone." 85 *Fed. Reg.* 72846 at 72884. It also required fiduciaries to report in detail their reasoning for using non-pecuniary factors. *Id.* These requirements ensured that investments were made primarily based on financial considerations, and to the extent other considerations were used, they were reported so that plan sponsors could hold their investment advisors accountable.

The 2022 Rule did away with these requirements. Contrary to the previous rule, it allowed non-collateral considerations when two competing investments "equally serve the financial interests of the plan over the appropriate time horizon." 87 *Fed. Reg.* at 73838. It also did away with the reporting requirements once associated with tiebreaker decisions. *Id.*

The 2022 Rule thus contravenes ERISA's assertion that the exclusive purpose of a fiduciary is to provide financial benefits, undermining the importance of financial interests with the modifying phrase "over the appropriate time horizon."

Under the new rule, small businesses who entrust others to make investment decisions for their employee retirement plans will find it more difficult to trust the integrity of those decisions. They will be forced to expend additional time and resources monitoring and reviewing recommendations from the plan's investment advisors, without the benefit of recordkeeping requirements, to ensure that advisors are focusing only on financial considerations and not collateral ESG factors. This is an unnecessary burden to place on small business owners, who should be able to trust that their retirement plans are a sound financial investment. The new rule—along with failing to protect plan sponsors and beneficiaries from risk-taking fiduciaries, as ERISA was meant to do—comes with an oversight cost that is not adequately measured.

Amici urge this Court to vacate the lower court's judgment and hold that the 2022 Rule violates ERISA.

ARGUMENT

I. The Phrase "Appropriate Time Horizon" is Vague and Opens the Door to Inappropriate Non-Financial Considerations.

The 2022 Rule effectively does away with ERISA's prioritization of financial interests by changing the tiebreaker test, granting a fiduciary the ability to make investment decisions based on collateral factors. It allows use of collateral considerations like ESG not only when two investments are *indistinguishable* as the previous rule had it, but also when they "equally serve the financial interests of the plan over the appropriate time horizon." 87 *Fed. Reg.* at 73885. The vagueness of this phrase is a departure from the clear tiebreaker envisioned in the previous rule, severely weakening the connection to financial considerations on its face—which is bad enough. To make matters worse, the phrase "appropriate time horizon" in this context further muddies the waters.

DOL's use of "appropriate time horizon" is not novel in itself—it appeared in the background of the 2020 Rule in the context of *not* using ESG factors. DOL said then that "fiduciaries should be focused on whether or not any given factor would materially affect the risk and/or return of the investment over an appropriate time horizon," 85 *Fed. Reg.* at 72858, and that they should concentrate on "providing participants with the financial benefits" and should exclude "imprecise and ambiguous ESG terminology" *Id.* DOL explained its reasons, stressing:

> The Department's continued concern about the growing emphasis on ESG investing that seeks to achieve non-pecuniary objectives or goals that are unrelated to the interests of the plan's participants and beneficiaries in their retirement income or financial benefits . . . and the consequence that ERISA plan fiduciaries may be prompted to make investment decisions for purposes distinct from providing benefits to participants[.]

Id.

Here, however, DOL has flipped that rationale on its head. Instead of using the phrase "appropriate time horizon" in consideration of pecuniary factors—explicitly *not* ESG—it now applies to non-pecuniary collateral factors—e.g., ESG. "Appropriate time horizon" here poses a definitional problem that it did not under the previous rule. Namely, if there are no longer such things as pecuniary or non-pecuniary factors, *see* 87 *Fed. Reg.* at 73826, then the definition of a financial interest has changed, and the question of what an appropriate time horizon is in relation to it becomes entirely uncertain. It does not help the search for an objective metric that an "appropriate" timeline is itself undefined and is therefore left open to a fiduciary's interpretation.[2]

Reading "over the appropriate time horizon" as modifying "financial interests of the plan" would mean that the question of whether a given investment is in the financial interest of the plan—a difficult determination itself without a clear delineation between pecuniary and non-pecuniary factors—might only be determinable over a period of years. Thus, the 2022 Rule may permit fiduciaries to rely on unreasonably lengthy time horizons to make unworthy investments more suitable.

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[2] The 2020 Rule is of little help here. In response to concerns that an "appropriate time horizon" might be too short, DOL allowed fiduciaries to define the term themselves: "The appropriate time horizon to consider for an investment or investment alternative can be plan specific, and the rule allows the plan fiduciary to make that determination for their plan." 85 *Fed. Reg.* at 72876.

The underlying ethos of ESG investing reveals the ways in which a potentially unlimited time horizon is ripe for abuse and presents a danger to plan sponsors and beneficiaries. A core principle behind the trend—in fact, the "E" in "ESG"—is that companies ought to take steps to reduce carbon emissions. Ajay Khari, *Why ESG Is So Difficult—And How To Implement It Successfully*, FORBES (Nov. 29, 2023, 3:30 PM), http://tinyurl.com/5n69p9f6. According to this idea, which is at the core of ESG, if carbon emissions are not reduced by 50% by 2030, the earth will undergo ecological disaster that will frustrate financial interests and throw economic systems into chaos and upheaval. *Goal 13: Take urgent action to combat climate change and its impacts,* UNITED NATIONS, http://tinyurl.com/bdtrvkxx (last visited Dec. 27, 2023).

Taking these predictions at face value, a fiduciary could consider any decisions companies make to alleviate or avoid contributing to climate change—even if the threat is far-off—to be in the financial interest of the plan. A fiduciary might find it "appropriate" to choose less financially viable investments that are, in his or her subjective estimation, better prepared for or actively working to avoid a future climate crisis.[3]

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[3] Though the 2022 Rule provides that a "fiduciary may not . . . accept expected reduced returns or greater risks to secure such additional benefits," 87 *Fed. Reg.* at 73885, the meaning of this limitation is equally obscure. It is unclear over what period an investment's expected returns would be considered reduced when financial considerations are themselves measured over an indeterminate "appropriate" time horizon.

Financial advisors serving as fiduciaries may be qualified to predict financial markets, but they are certainly unqualified to predict fluctuations in the global climate. The Supreme Court has emphasized that "predicting future climate change necessarily involves a complex web of economic and physical factors" that include:

> predict[ing] future global anthropogenic emissions . . . the fate of these emissions once they enter the atmosphere . . . the impact of those emissions that remain in the atmosphere on the radiative properties of the atmosphere; changes in critically important climate feedbacks . . . changes in temperature characteristics . . . changes in other climatic parameters . . . and ultimately the impact of such changes on human health and welfare[.]

Massachusetts v. E.P.A., 549 U.S. 497, 544 (2007) (internal citation omitted). There is no basis for believing that ERISA fiduciaries possess the necessary scientific and technical knowledge to make such assessments. Yet DOL suggests that they do.

This runs counter to reason. Climate science is imprecise and even for experts, climate change can be difficult to predict. The oft-repeated mantra today is that we have until 2030 to reduce carbon emissions to avoid disaster. Yet in 1972, a UN environmental protection official said that there were just "ten years to stop the catastrophe." *50 years of predictions that the climate apocalypse is nigh,* THE NEW YORK POST (last updated Nov. 12, 2021, 6:08 PM), http://tinyurl.com/8wjadzw2. In 1989—seventeen years later—another UN official predicted that "entire nations could be wiped off the face of the Earth . . . if the global warming trend is not reversed by the year 2000." *Entire Nations Could Disappear Beneath the Rising Oceans*, FINANCIAL REVIEW (Jun. 30, 1989, 10:00 AM), http://tinyurl.com/29xumpwb. In 2005—long after entire nations were supposed to be destroyed by climate change—UN experts predicted that there would be 50 million climate refugees by 2010. David Adam, *50m environmental refugees by end of decade, UN warns,* THE GUARDIAN (Oct. 12, 2005, 9:32 AM), http://tinyurl.com/yneahwx6. By 2012—two years after the failure of that prediction—scientists predicted that the Arctic would be ice-free by 2016. John Vidal, *Arctic expert predicts final collapse of sea ice within four years,* THE GUARDIAN (Sep. 17, 2012, 6:14 EDT), http://tinyurl.com/n4muezbe. And today it appears we have yet another ten years before that prediction comes true. Chelsea Harvey and E&E News, *An Ice-Free Arctic Could Be Only a Decade Away,* SCIENTIFIC AMERICAN (June 7, 2023), http://tinyurl.com/2khvz9ew. When even climate experts struggle to make predictions on an accurate timeline, investment managers and financial advisors cannot be expected to make similar predictions and properly integrate factors such as climate change over an uncertain time horizon.

The point of ERISA is not to predict climate disaster or further sustainability goals in the hopes that these values will one day coincide with beneficiaries' financial interests. Instead, it is to further financial interests, period. This Court should reaffirm that understanding and reject the 2022 Rule's modification of the tiebreaker test. Alternatively, to the degree that the Court sees fit to read the phrase "appropriate time horizon" innocuously, it should be construed narrowly in a way that eliminates far-off future hypotheticals about climate disaster from the considerations that are appropriate to a fiduciary of a retirement plan.

II. The Rule Places an Extraordinary Oversight Burden on Small Businesses Who Provide Employee Retirement Plans.

The 2022 Rule, and the district court opinion upholding it, ignores the hardship that small businesses face when ESG factors are placed on equal footing with financial interests. Namely, business owners—who often rely on financial advisors and firms to manage their employee retirement plans—must closely observe the investments that their advisors choose, running the risk that these advisors will prioritize collateral ESG factors rather than purely financial interests in choosing investments. Indeed, the 2022 Rule fails to acknowledge in its Regulatory Flexibility Act analysis the increased costs that will fall upon small businesses in having to engage in increased oversight of their fiduciaries. *See* 87 *Fed. Reg.* at 73882.

Financial interests are especially paramount in the management of employer-sponsored retirement plans. When a small business contracts with outside experts to choose its retirement plan's investments, the business owner is primarily concerned with the chosen investments' economic performance so they can fund the plan and offer it as an attractive employee benefit. Providing useful benefits helps businesses to draw in workers, a major concern for business owners.[4] If small businesses can rely on fiduciaries to make investments based purely on financial considerations, then retirement accounts remain a benefit that can draw in employees at a critical time.

However, when fiduciaries are allowed to make decisions based on ESG, this confidence is compromised, because ESG investments perform poorly and fail to outcompete non-ESG funds. Sanjai Bhagat, *An Inconvenient Truth About ESG Investing*, HARVARD BUSINESS REVIEW (March 31, 2022), http://tinyurl.com/yu7tv5nf. In 2022, "the 10 largest ESG funds by assets . . . all posted double-digit losses." Tim Quinson, *Big ESG Funds Are Doing Worse Than the S&P 500*, BLOOMBERG (Dec. 7, 2022), http://tinyurl.com/3xnxkazp. ESG funds are riskier, leaving investors "more susceptible to volatility and lower future returns than if they had parked their money in a vanilla, unthemed index fund." Taylor Tepper, *It's Not Easy Being Green: Why Is ESG Underperforming In 2022?*, FORBES (Feb. 17, 2022, 8:07 AM), http://tinyurl.com/49w4csm2.

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[4] Locating qualified employees remains a problem that businesses rank as their number two priority. NFIB Research Center, *Small Business Problems & Priorities*, at 9 (2020) https://bit.ly/44np6Oz. In October 2023, a net 36% of NFIB member small business owners reported raising compensation in order to find qualified applicants. *See* NFIB Research Center, *Small Business Unfilled Job Openings Remain In the Historical Stratosphere* (NFIB October Jobs Report) https://tinyurl.com/yhcap9ja (last visited Dec. 5, 2023).

This poor economic performance does not occur in a bubble—as a result, 32 ESG funds plan to close. Shane Shifflett, *Wall Street's ESG Craze Is Fading*, THE WALL STREET JOURNAL (Nov. 19, 2023, 5:30 AM), http://tinyurl.com/3rxpzcfs. Investors have noticed, withdrawing more than $14 billion from ESG funds in 2023. *Id.* A fiduciary basing a long-term investment strategy on a trend like ESG would be irresponsible given these metrics, yet the 2022 Rule allows them to do so.

Engaging in minutia-level oversight is now a practical necessity for small businesses, whose employee retirement plans depend on advisors making decisions on financial rather than ESG factors. Yet the need to provide additional oversight to financial advisors will be yet another in a long list of tasks that drain a small business owner's time and resources. 64 percent of them do their own bookkeeping. NFIB Research Center, *NFIB National Small Business Poll Tax Complexity and the IRS* (2017), https://tinyurl.com/yc2snjvu. Only 12 percent have a dedicated human resources professional. NFIB Research Center, *NFIB National Small Business Poll Business Structure* (2004), https://tinyurl.com/5dy54jv6. Nearly half of small businesses do payroll, financial paperwork, and recordkeeping in-house. *Id.* Further, businesses spend about 200 hours per year just on regulatory compliance, and on average it costs small businesses with fewer than 20 employees 60% more to do so than it does large companies. Abigail Thorpe, *Infographic: The Cost of Compliance*, NFIB.com (Oct. 24, 2016), https://bit.ly/3qa1P32. In effect, small business owners are already serving as accountants, record custodians, HR professionals, and do-it-yourself lawyers, all while running a business.

Given that they do not have the resources—especially the time—to become investment experts as well, it makes sense that they would trust others to help them run their employee retirement plans. Under the 2022 Rule, however, this arrangement becomes untenable. Plan sponsors are likewise considered fiduciaries under ERISA and are liable for the poor decisions of investment advisors. If business owners can't trust their advisors, their only alternatives are to spend time and money they don't have to gain investment expertise, or else to stop offering retirement plans entirely.

Considering these increased risks and burdens, the 2020 Rule indicated that plan sponsors, including small businesses, are due an increased level of information to ensure that their fiduciaries are making well-informed investment decisions. If a fiduciary made an investment decision not based on financial factors, the rule required fiduciaries to report:

> (i) Why pecuniary factors were not sufficient to select the investment . . . (ii) How the selected investment compares to the alternative investments . . . and (iii) How the chosen non-pecuniary factor or factors are consistent with the interests of participants and beneficiaries in their retirement income[.]

85 *Fed. Reg.* at 72884. These requirements were so stringent because, aside from breaking a tie, a "fiduciary's evaluation of an investment or

investment course of action must be based *only* on pecuniary factors." *Id.* (emphasis added). This understanding is consistent with ERISA, which requires that fiduciaries act for an "exclusive" financial purpose, *see* 29 U.S.C. § 1104(a)(1). Thus, the tiebreaker was a fail safe for when financial factors alone were insufficient, and the reporting requirements ensured that businesses could verify the integrity of those decisions.

The 2022 Rule ignores that purpose entirely, instead jettisoning the reporting requirements because their use "suggest[s] that ESG investing entails extraordinary risks" and may "chill and discourage plan fiduciaries from using the tiebreaker test generally, including in cases involving the appropriate consideration of ESG . . . " 87 *Fed. Reg.* at 73838. But a chilling effect is a feature, and not a bug, of the tiebreaker test and its reporting requirements. The tiebreaker test *should* be used sparingly, only in those situations where a fiduciary is caught between two equal-on-paper investments, especially given the limitations set forth in ERISA. And as discussed above, ESG investing does entail extraordinary risks from which plan sponsors need protection.

In fact, ERISA was enacted to prevent this kind of excessive risk-taking. One of ERISA's primary purposes was to ameliorate concerns that the "soundness and stability of plans with respect to adequate funds to pay promised benefits may be endangered." 29 U.S.C. § 1001(b). DOL understood this when it promulgated the 2020 rule, which sought to prevent fiduciaries from "subordinat[ing] the interests of the participants and beneficiaries in their retirement income or financial benefits under the plan to other objectives," thereby "sacrific[ing] investment return or tak[ing] on additional investment risk to promote non-pecuniary benefits or goals." 85 *Fed. Reg.* at 72884. Yet the 2022 Rule has abandoned the pecuniary distinction, *see* 87 *Fed. Reg.* at 73826, and will force those who ought to be protected under ERISA to set their own standards and engage in their own monitoring. DOL's construction of ERISA therefore undermines its express purpose.

This Court should hold that fiduciaries cannot make investment decisions based on collateral factors, especially without having to report their reasoning. It should reject the implausible notion that ERISA allows the creation of standards that don't protect plan sponsors and requires them to engage in costly oversight. *See Am. Tobacco Co. v. Patterson*, 456 U.S. 63, 71 (1982) ("Statutes should be interpreted to avoid untenable distinctions and unreasonable results whenever possible."). *See also Shell Offshore, Inc. v. Tesla Offshore, L.L.C.*, 905 F.3d 915, 921 (5th Cir. 2018) ("We will avoid interpreting a statute to produce absurd results if alternative interpretations consistent with legislative purpose are available." (internal quotations omitted)).

Businesses depend on a restrained use of the tiebreaker test, and the reporting that it previously required, to monitor fiduciaries' investment decisions easily and effectively. DOL has instead created a free-for-all regime that empowers fiduciaries, contrary to the statute, to make poor investments without even a paper trail for plan sponsors to hold them accountable. ERISA must keep fiduciaries in check, rather than businesses having to do it themselves.

CONCLUSION

For the reasons above, *Amici* urge this Court to vacate the decision below.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on January 25, 2024, I electronically filed the foregoing document with the Clerk of the Court for the U.S. Court of Appeals for the Fifth Circuit by using the appellate CM/ECF system, which will serve all parties in this matter.

/s/Christian Townsend
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CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because it contains 3,697 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(f).

This brief also complies with the type-face requirements of Fed. R. App. P. 32(a)(5)(A) and the type-style requirements of Fed. R. App. P. 32(a)(6) because it has been prepared in a proportionally spaced type-face using Microsoft Word in Century Schoolbook font size 14.

/s/Christian Townsend
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