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Subcommittee on Economic Growth, Energy Policy, and Regulatory Affairs

and the

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"The Impact of ESG Policies on American Investors, Retirees, and Pension Plans"

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Mr. Chairman, Madam Chairwoman, and distinguished members of the House Oversight Committee. Thank you for the opportunity to testify on a financial issue of great significance to the tens of millions of American retirees and the tens of millions more Americans who will soon be retired: The Impact of ESG investment and federal ESG policies on Americans' investment returns on their lifetime savings.

In compliance with Truth in Testimony, I attest that neither I nor my employer receive any funding form the United States federal government.

In this testimony, I would like to emphasize two points, based on studies I have been involved with that deal with ESG policies.

First, when it comes to ESG investing, there is little doubt that when fund managers restrict the kinds of investments they make -that are not related to increasing the returns to their clients, they are violating their fiduciary duty and should be held accountable for potential fraud.

Second, the analysis that I participated in this year of ESG proxy voting finds most of the nation's major money management firms, with multiple trillions of dollars of Americans' lifetime savings are routinely violating that fiduciary. ESG resolutions and ESG investing on balance UNDERPERFORM the stock market and therefore can cost average families tens of thousands of dollars by achieving lower returns. ESG proxy voting is happening routinely without the consent or even knowledge of the clients whose money they are safeguarding.

How Prevalent Is ESG Investing Work?

Investment management companies – including J.P. Morgan, Blackrock, and Fidelity - have trillions of dollars of Americans' lifetime savings under management. These companies indirectly own roughly 75 percent of the shares of America's publicly traded corporations. These money managers also have a legal obligation to earn the highest return for the tens of millions of Americans, who have placed their lifetime savings and pensions in these firms' legal custody.

But our new Committee to Unleash Prosperity study “Putting Politics Over Pensions” finds that a majority of the largest firms are routinely violating that fiduciary duty and letting political biases interfere with sound business practices.

Through a process known as “proxy voting” money management firms like State Street are voting on shareholder resolutions of the companies their clients own. Without the support or even the knowledge of their clients, big money managers are routinely supporting resolutions brought by leftist social activists. These “ESG’ resolutions – which stands for “environment,” “social justice,” and “governance”- impose on a company’s management radical climate change mandates – such as zero carbon emissions - divestment of oil and gas, or plastics companies, racial and gender quotas in hiring and so on.

This practice hurts American retirees and investors because myriad studies have indicated that ESG policies typically reduce shareholder returns. For example, when firms were required to sell their oil and gas holdings, this cost their clients potentially tens of thousands of dollars in returns because companies like Chevron and Exxon had among the highest returns in 2022. I have no problem with Americans choosing to put their money in funds that are explicitly ESG funds.

Our study has found that a majority of the 40 largest investment firms voted routinely in favor of even the most invasive ESG proposals related to related to left-wing environmental and equity activism. None of these proposals were supported by management at the targeted companies.

The table below shows the results of the 40 largest investment firms, which account for the vast majority of funds under management. Vanguard and Dimensional earned the best grades, having voted in the interests of their clients at least 90 percent of the time.

But a grade of F- went to six firms that supported more than 90 percent of ESG-focused shareholder resolutions:

- Deutsche Bank

- Swisscanto
- Northern Trust
- Storebrand Asset Management
- Invesco Perpetual Select Trust
- BNP Paribas

Nine other notable firms earned a D or an F:

- Columbia Threadneedle
- AllianceBernstein
- Geode
- Invesco Capital
- Guggenheim
- State Street
- Sun America
- Royal Bank of Canada
- Wellington

By voting with shareholder activists on resolutions that are hostile to the company's ability to provide a high return to shareholders, the result is billions of dollars in losses for America's shareholders – a high price to pay for advancing a leftist agenda they were never asked whether they support. The losses we all suffer will not just be from lower share prices: America's security and global competitiveness depend on its corporations' leadership.

What is ESG Investing?

ESG investing is a disingenuous response by the left to its failure to enact its unpopular social policies (like race-based hiring) and its environmental agenda. Having failed through the open political process to directly impose mandates on businesses, the tactic now is to try to foist its ideas on companies through an opaque process that leverages the money of others to hijack corporate governance.

ESG investing is becoming more common in the investment world. The process involves pension funds, endowments, and investment firms wielding their influence at shareholder meetings to support left-leaning measures related to race, sex, ethnicity, the environment, and political activity. These large firms exercise this influence through what’s known as “proxy voting,” in which the aforementioned entities vote the shares of their clients on proposals advanced primarily by liberal activist groups.

In recent years, left-leaning activist groups have become much more aggressive at shareholder meetings and are filing more resolutions and pursuing bolder, more audacious objectives. They hide extreme positions behind anodyne terms such as “diversity,” “racial equity,” and “climate justice.”

Emblematic of how a fund manager can go awry is USAA, whose capital is invested through its partner, Victory Capital. It earned an F-,surely not reflecting the views of their investors, who are limited to members of the military and their descendants. Meanwhile, an F was also the average grade earned by the 31 public pensions and endowments that cast votes on the Fiduciary-Free 50. (See methodology below.)

A striking contrast was Vanguard, which recently opted out of its membership in the Net Zero Asset Managers Initiative. It earned an A grade.

Fund families receiving an F

The following 25 of the most active voting firms earned an F, based on their voting records within non-ESG branded funds on the Fiduciary-Free 50 proposals.

- DWS Investment GmbH
- Swisscanto
- Guggenheim Investments
- MFS Investment Management, Inc.
- American Century
- Thrivent Investment Management, Inc.
- UBS Asset Management
- Northern Trust Investments
- Storebrand Asset Management
- Invesco Perpetual Select Trust Plc
- BNP Paribas Asset Management
- First Trust Advisors LP
- ProFund Advisors LLC
- DWS Investment Management Americas, Inc.
- Danske Bank A/S
- Credit Suisse Asset Management LLC

- Gotham Asset Management, LLC
- TD Asset Management
- Victory Capital Management, Inc.
- Irish Life Investment Managers Limited
- ProShares
- Principal Global Investors LLC
- APG
- United Services Automobile Association (USAA)
- Parametric Portfolio Associates, LLC

The funds receiving an A grade were:

Dimensional Advisors

Vanguard

Fidelity

T.Rowe Price

ESG Funds Underperform and Are De Facto Violations of Fiduciary Duty

The fundamental issue with ESG and related measures is that in most cases, they have a proven record of undermining company performance and shareholder returns. And that creates a thicket of liability issues for pensions and fund families that support these measures, given that state and federal law requires pensions and fund families to focus on maximizing shareholder returns.

The Biden Administration and many liberal activists and academics contend that ESG investing increases a company's returns by lowering the risk of climate change weather events or by promoting racial and gender equality. But numerous studies show that those returns are depressed (through stock price performance and the burden of higher fee structures charged to investors), add costs to companies, and deviate from core competencies when pursuing an ESG agenda.

- A meta-review of more than 2,000 studies found that ESG-focused investing depressed returns.[1]

[1] https://www.tandfonline.com/doi/full/10.1080/20430795.2015.1118917

- A performance review conducted by Boston College and published in 2020 found that pension funds with an ESG orientation lagged those of non-ESG funds by two basis points per year over a ten-year period.[2]

- A 2022 Harvard Business Study concludes: "Investing in sustainable funds that prioritize ESG goals is supposed to help improve the environmental and social sustainability of business practices. Unfortunately, close analysis suggests that it's not only not making much difference to companies' actual ESG performance, it may actually be directing capital into poor business performers."

- In a recent Journal of Finance paper, University of Chicago researchers analyzed the Morningstar sustainability ratings of more than 20,000 mutual funds representing over $8 trillion of investor savings. Although the highest rated funds in terms of sustainability certainly attracted more capital than the lowest rated funds, none of the high sustainability funds outperformed any of the lowest rated funds.

- In 2022, many ESG proposals to banks and insurance companies attempted to halt any financing or underwriting activities that could have supported new fossil fuel projects. But the oil and gas sector outperformed nearly every other industry, in terms of stock market gains.

What Should Be Done to Protect Investors

Congress should investigate whether the financial firms with trillions of dollars under management are honoring their fiduciary duty to their clients. If they are not, they may be committing investor fraud. These firms have an obligation to get the best return for their clients – not to save the planet. If individual investors want their retirement dollars invested in ESG, there are hundreds of plans that explicitly make those kinds of investments.

It is worth noting that states are already taking action. Nineteen state attorneys general wrote to BlackRock's Fink last year and questioned whether the company was violating its fiduciary and legal obligations:

[2] ESG Investing and Public Pensions: An Update (bc.edu)

> Blanket statements regarding investing in particular asset classes without referencing price is not consistent with fiduciary and legal obligations. Nor are blanket commitments to vote for directors based upon protected characteristics, such as gender. Rather, BlackRock appears to be acting for a social purpose that may have a financial benefit if certain improbable assumptions occur. If BlackRock were focused solely on financial returns, its conduct would likely be different.[3]

To avoid legal liability, BlackRock maintains that "We are a fiduciary. . . .We put our clients' interests first and deliver the investment choices and performance they need."[4]

But the ideological hijacking of the fiduciary obligation by companies like BlackRock and other fund families is undeniable. Just this week BlackRock's CEO Larry Fink reiterated the commitment to forcing firms to adopt ESG policies – whether it is in the interests of shareholders or not.

Does ESG Reduce Future Risks?

At the heart of the ESG movement is the assumption that all of the future risks to the economy and the state of the planet emanate from climate change risks and the use of fossil fuels. Those risks exist. And there are ecological and financial risks from every other form of energy. But there are enormous risks and costs to NOT producing American oil and gas, or plastics, or coal, or pipelines, etc. Technological development and economic growth are by far the best ways to combat ecological risks. Similarly, racial and gender quotas are inconsistent with the concept of merit based on performance and qualifications.

Biden's Anti-Fossil Fuels ESG Agenda Is Making America Poorer

The worst example of how ESG fanaticism is negatively impacting Americans is the rise in oil and gas prices at the pump and the impact on prices and U.S. GDP.

The Biden administration's hostility toward the oil and gas industry is well-established. The Institute for Energy Research has chronicled more than 100 separate actions and orders by the Biden administration that have blocked or created financial disincentives for drilling.

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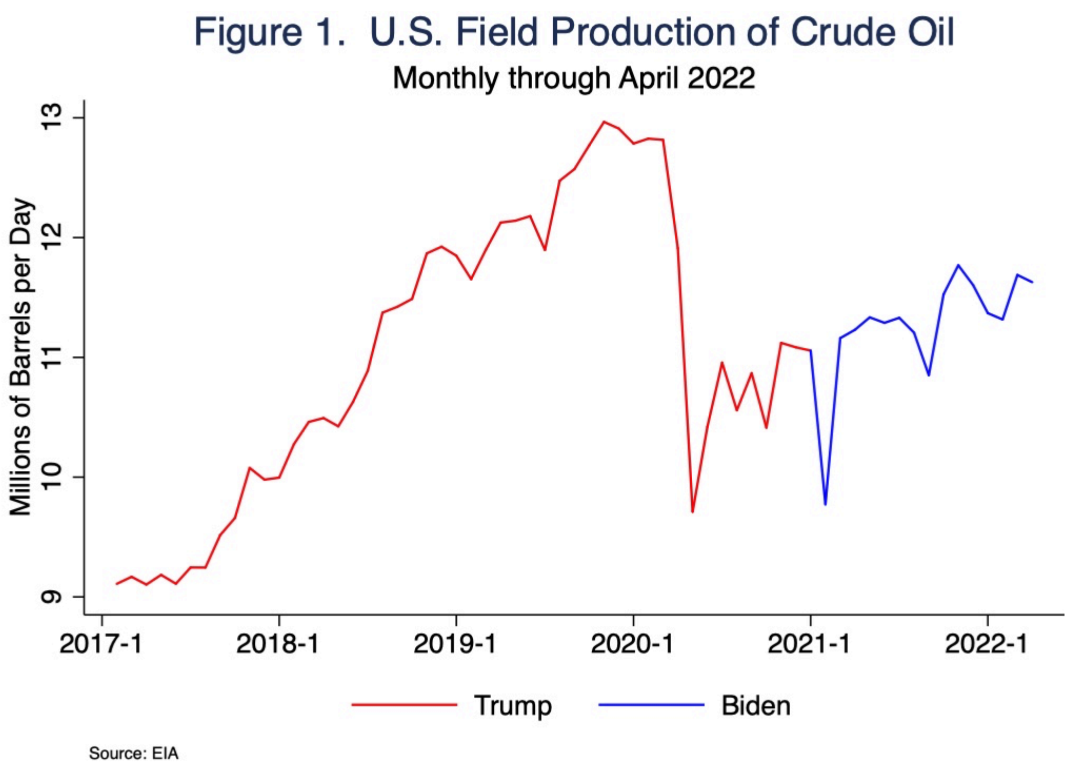
[3] BlackRock Letter.pdf (texasattorneygeneral.gov)

[4] https://abcnews.go.com/Business/esg-investing-republicans-criticizing/story?id=97035891

As the graph below shows, by January 2021, the U.S. had achieved Trump's goal of energy independence. That is to say, the U.S. was a net EXPORTER of oil and gas. The Energy Information Agency had predicted that the U.S. could produce as much as 15 million barrels of oil under current trends.

Another data point: in early 2020, right before the Covid crisis shutdown the American economy, the United States oil and gas industry reached peak production at a record 13 million barrels of oil a day, according to the U.S. Department of Energy's Energy Information Administration (EIA).



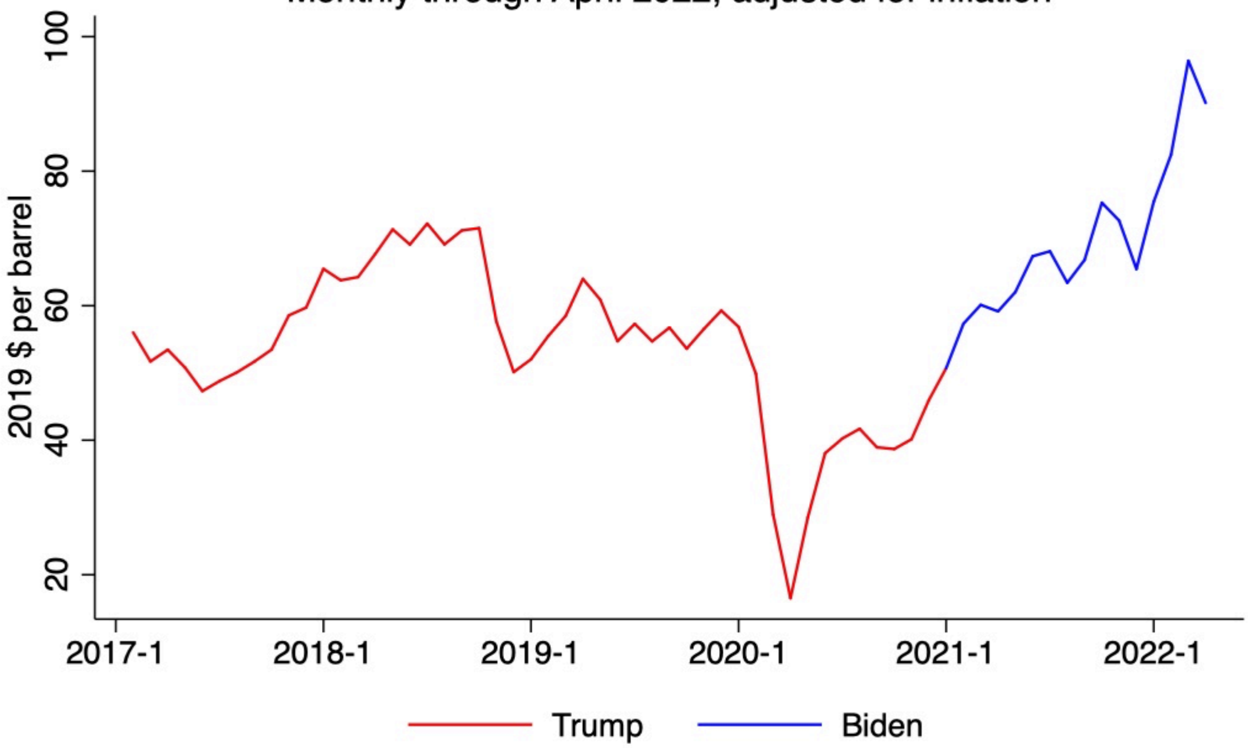
According to EIA, in April of 2023 (the latest U.S. data available), U.S. oil production was roughly 12 million barrels. This is assuredly LESS than the 13 million peak we reached under Trump.

Our best guess is that production is down by between 1 to 1.5 million barrels today from the Trump peak. At $80 a barrel, this is a loss of output to the tune of roughly $100 million a day in lost U.S. economic output.

But that is NOT the end of the story. The price of oil today is MUCH higher than the price when Trump was president. Adjusted for inflation, the average world price throughout Trump's presidency was $54 a barrel, and rarely exceeded $65. During Biden's presidency, the average was $71 through April 2022 and averaged $86 in 2022. See Figure 2.

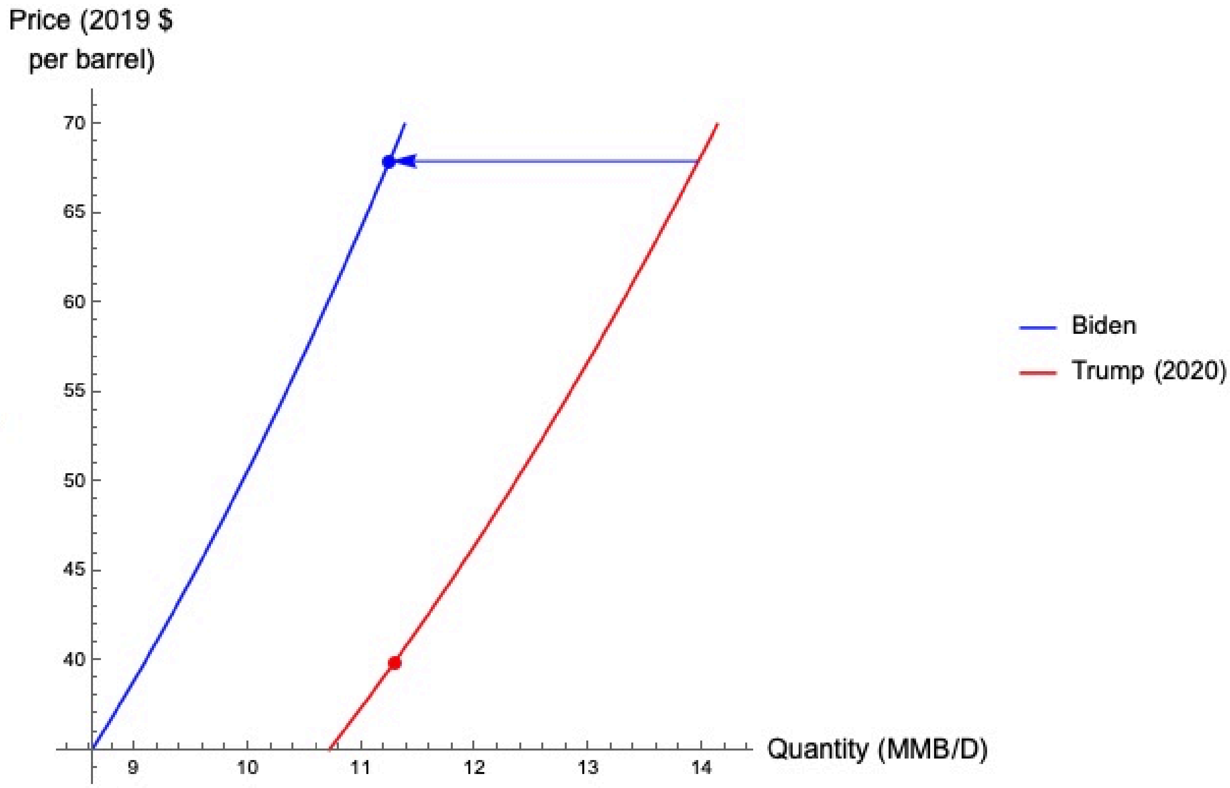
Figure 2. Oil prices

Monthly through April 2022, adjusted for inflation



Source: EIA data on Cushing OK WTI Spot Price FOB

Figure 3. Something reduced the supply of oil after 2020



Circles are actual price-quantity points.
The supply shift (arrow) is -2.5 MMB/D in the quantity dimension.
Supply elasticity of 0.4 from US EIA.

Our estimate is that if the Trump supply conditions had remained in place, daily U.S. oil production from 2021-23 would have been roughly two million barrels, and daily gas production 20 billion cubic feet, greater. The U.S. would again be the lead energy producer.

Under that scenario, the U.S. would not have to import a single net barrel of oil from abroad. The U.S. would be producing at least $200 million more oil output per day.

This is a direct hit on the American economy that equates to between $100 and $200 billion a year-depending on the fluctuation of the world price of oil and gas. ESG investing ("Environmental, social, and governance") requirements pile on obstacles and costs to U.S. production. They are making America poorer and shifting production to our adversaries – with no net benefit to the environment.