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October 5, 2020

Ms. Jeanne Klinefelter Wilson
Acting Assistant Secretary
Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Avenue NW
Washington DC 20210

RE: Fiduciary Duties Regarding Proxy Voting and Shareholder Rights Proposed Rule RIN 1210-AB91

Dear Acting Assistant Secretary Klinefelter Wilson:

Segal Advisors, Inc., d/b/a Segal Marco Advisors ("Segal Marco") appreciates the opportunity to comment on the proposed rule, *Fiduciary Duties Regarding Proxy Voting and Shareholder Rights* ("Proposed Rule"), which seeks to amend the duties and obligations related to the exercise of shareholder rights for ERISA-covered plans, including proxy voting, the use of written proxy voting policies and guidelines, and the selection and monitoring of proxy advisory firms.

Segal Marco has long held that proxy votes are an important lever for investors, including ERISA plans, to express their views to issuers for the purpose of protecting and ultimately enhancing the investor's value. In our view, the Proposed Rule significantly weakens this lever, unnecessarily raises costs to plan investors and threatens to undermine an important check and balance on corporate governance at U.S. publicly held issuers. We therefore urge the Department of Labor (the "Department") not to adopt the Proposed Rule or to rework and repropose the rule in a form that both recognizes the important check on corporate governance and provides greater protections and flexibility for ERISA plan fiduciaries in exercising these rights on behalf of plans.

Background

Segal Marco is an SEC-registered investment adviser. We provide investment advisory, consulting and related services to more than 700 employee benefit plans regulated under ERISA, with a particular focus on serving the multiemployer plan market. We also provide similar services to more than 100 benefits funds that are not technically covered by ERISA, but generally look to ERISA as a guide for conducting plan activities and engaging plan service providers.

Segal Marco's Perspective on the Proposed Rule

The Department expressed concern that "some fiduciaries and proxy advisory firms—in part relying on the Avon Letter—may be acting in ways that unwittingly allow plan assets to be used to support or pursue proxy proposals for environmental, social, or public policy agendas that have no connection to increasing the value of investments used for the payment of benefits or plan administrative expenses, and in fact may have unnecessarily increased plan expenses."[1] The citation underpinning this assessment is a summary of an audit published by the Department's Office of Inspector General in 2011.[2] This audit found that plans did not generally document: (1) their proxy voting decisions or (2) an economic benefit for proxy voting decisions. At the time, the Assistant Secretary for Employee Benefits Security, reacting to the audit's findings and recommendations "did not believe proxy-voting activities warranted specific legislative changes, specific documentation requirements, nor increased enforcement activities."[3]

In our experience, proxy voting service provides do provide, or otherwise already make available to their clients, these types of documents and engage in a rigorous process when making decisions about proxy voting. Therefore, we believe the Proposed Rule is unnecessary.

For example, where we are engaged to provide proxy voting services as a plan fiduciary, we:

- provide each such client with periodic reports, discussing significant details about particular proxies, including how each vote was cast during the reporting period and the rationale for our decision.
- cast votes in accordance with the clients' formal proxy voting policies and directions, subject to our ultimate fiduciary responsibilities as required under ERISA.
- regularly consider whether changes to the client's policy should be considered.
- provide an annual summary of market developments and regulatory changes.

Moreover, technological advances, particularly since the 2011 audit's conclusion, have materially eased the burden on proxy voting transparency, as voting and related documentation has almost entirely migrated to web-based platforms that now capture, accumulate and generate reports in near real time. Given these new systems and the advances since the 2011 audit, plans, like all institutional investors, should have access to and be able to produce voluminous reports

[1] Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, (Proposed Rule.) Employee Benefits Security Administration., RIN 1210-AB91, page 55223, available at: https://www.federalregister.gov/documents/2020/09/04/2020-19472/fiduciary-duties-regarding-proxy-voting-and-shareholder-rights#footnote-41-p55222.
[2] U.S. Dep't of Labor Office of Inspector General Report No. 09-11-001-12-121, Proxy-Voting May Not be Solely for the Economic Benefit of Retirement Plans (Mar. 31, 2011), www.oig.dol.gov/public/reports/oa/2011/09-11-001-12-121b.pdf.
[3] Ibid.

and audit trails on their proxy voting activity upon request. These reports and information should provide the plan fiduciaries with all the documentation needed to monitor the plan's proxy voting activities.

Further, many plans utilizing proxy voting services, host periodic meetings for the plan fiduciaries to review a plan's proxy voting activity and policy (including potential changes thereto).

Based on our experiences and observations, plan fiduciaries take their proxy voting responsibilities seriously, and have implemented processes to ensure that they are vetting for both an understanding of what is happening with the issuer and how best to protect the plan's investment in the issuer.

We believe and support policies and disclosures that are linked to enhanced standards and best practices of enhancements to corporate governance as is typically outlined in our clients' proxy voting policies. We believe that the benefits of proxy voting on overall corporate governance must be viewed and evaluated in the aggregate, as opposed to on a proxy-by-proxy, plan-by-plan basis. We are supportive of guidance to support that plans are not required to incur extraordinary costs to vote a proxy where the cost/benefit analysis clearly does not warrant such a plan expense (*e.g.* proxies for certain foreign issuers).

We note, for example in regards to board independence, that certain investors believe that companies with a governance structure where a significant portion of the board is independent of management are likely to outperform similar companies without this type of board independence. There is no proxy vote directly on the question of whether a board of directors should be independent or not. Instead, investors typically address the merits of board independence in the proxy voting policy and then vote for governance mechanisms that increase the likelihood of independent nominees. Those associated proposals include:

- adopting a majority vote standard for the election of a director;
- declassifying the board to require each director stand for election annually;
- disclosure of a qualification matrix for board skills; and
- board refreshment policies including a mandatory retirement age for directors.

Moreover, regular proxy voting supports a healthy and vibrant U.S. equity market, which is a priority for all investors (including plans) by providing a mechanism for real-time investor feedback, which enables corporate managers to make informed decisions under investor oversight. As a notable business group argues, a perception that investors are unable to hold corporate managers accountable weakens the system. The Committee for Economic Development of The Conference Board ("CED") is a nonprofit, nonpartisan, business-led public policy organization that provides analysis and solution to the nation's critical issues. In a 2009 report, the CED stated, "The business and academic leaders who comprise CED are unwavering advocates for the free market system, and just as firm in the belief that business and their leaders must earn the public's trust. Perceptions that firms flout rules, behave unethically, and use deceptive business processes weaken confidence in, and support for, the free enterprise system. Executive compensation untethered to economic value violates perceptions of fairness, leads to mistrust, and courts a stifling regulatory backlash."[4]

Investors concerned about systemic risks, trends and changes facing an issuer and its business have but three actionable steps available to address their concerns:

- divest or tilt the portfolio away from these companies that may be operating well in the current environment but are lax in responding to the investor's outward concerns on particular risk factors;

- vote proxies in support of disclosure and assessment to inform management of the significance of said risk factors; or

- engage companies through shareholder proposals or other means to gauge their perspective on and plans for responding to risk factors.

Without the latter two tools, investors' only reasonable response to such risks (which could impair the value of a plan's investment) will be through asset sales, which could be costly to both the issuer and the investor. Moreover, removing these tools removes a valuable and cost-effective feedback and oversight mechanism for corporate America.

As another example, a vast body of research and the SEC's own regulatory guidance demonstrates that diversity has an economic impact.[5] The application of that support within proxy voting lies squarely in our ability to vote in favor of shareholder proposals that: (1) focus on diverse human capital and talent in corporate governance; (2) propose that companies adopt diverse recruitment standards; and (3) oppose nominating committee members where a board lacks diversity. The economic benefit is not outlined in each rationale for every vote but rather lives in the proxy voting policy. The Proposed Rule would undermine this pragmatic and cost-effective approach by requiring a specific cost-benefit analysis for each vote, thereby increasing the costs associated with voting proxies for ERISA plans. Moreover, the economic benefit of diversity, while proven through research, may be challenging to objectively quantify as the Proposed Rule would seem to require, which may cause ERISA plan fiduciaries to weigh in favor of abstaining from these votes.

Segal Marco appreciates the Department's acknowledgement that conducting cost-benefit analysis on individual proxy votes "may often burden fiduciaries out of proportion to any

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[4] "Corporate Governance Practices to Restore Trust, Focus on Long-Term Performance, and Rebuilding Leadership." Committee for Economic Development. February 11, 2009, available at: https://www.ced.org/reports/corporate-governance-practices.

[5] A January 2015 study by McKinsey & Company, "*Why Diversity Matters,*" found companies in the top quartile for gender or racial and ethnic diversity tend to report financial returns above their national industry medians.
Credit Suisse came to similar conclusions in its 2014 study, "*Women's Positive Impact on Corporate Performance.*" The financial services firm found "Greater gender diversity in companies' management coincides with improved corporate financial performance and higher stock market valuations."
Proxy Disclosure Enhancements (Final Rule). Securities and Exchange Commission. File No. S7-13-19, available at: https://www.sec.gov/rules/final/finalarchive/finalarchive2009.shtml. See: "We agree that it is useful for investors to understand how the board considers and addresses diversity, as well as the board's assessment of the implementation of its diversity policy, if any."

potential benefit to the plan."[6] However, we do not agree that the three permitted practices outlined in the Proposed Rule are viable options for most plans. The Department states the practices are "thereby allowing plans to focus resources on matters most likely to have an economic impact." **However, the Department offers no evidence that the matters cited have an economic impact. Nor does the Department provide any evidence that matters not cited fail to have an economic impact. Rather, we are left with a short list of select issues that have no demonstrated importance superior to all other proxy voting items.** Moreover, while a set of permitted practices may be useful if structured as a safe harbor, the Proposed Rule would still require fiduciaries to override the practice where the costs and benefits of voting or not voting suggest a different decision, thus undermining any protections or efficiencies these practices may otherwise create.

The permitted practices enumerated are: (1) plans adopt a proxy voting policy to always **vote with management's recommendation**; (2) plans adopt a proxy voting policy to **only vote on corporate events** (mergers and acquisitions transactions, dissolutions, conversions, or consolidations, corporate repurchases of shares (buy-backs), issuances of additional securities with dilutive effects on shareholders, or contested/ elections for directors; or (3) plans adopt a proxy voting policy to **refrain from voting proposals** when the plan's holdings of the issuer relative to the plan's total investment assets is below quantitative thresholds that the fiduciary prudently determines, considering its percentage ownership of the issuer and other relevant factors, is sufficiently small that the matter being voted upon is unlikely to have a material impact. The Department suggests a five-percent cap may be the appropriate marker.

Our concerns with each of these approaches are discussed below.

Always Voting With Management's Recommendations

A practice of voting with management may bias fiduciaries towards the sponsor of the proposal. Both shareholders and management are able to sponsor proposals. Should a plan support a proposal when sponsored and recommended by company management, but vote against, or not vote on, the same proposal if sponsored by a shareholder?[7] Would a cost/benefit analysis of a majority voting proposal yield different results depending on who was asking the question? The answer to both questions is likely no.

The evidence from the 2008 global financial crisis as well as more recent controversies involving Facebook, Wells Fargo and Boeing, et al, show corporate directors are capable of poor judgement. We believe that weakened participation in proxy voting under any of the permitted practices could result in a lack of management accountability to shareholders that is destabilizing. The Proposed Rule seems to suggest a contradictory standard for plan fiduciaries, who would be required to increase their due diligence on proxy advisory firms consistent with

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[6] Ibid. page 55225.
[7] Allen, Claudia H, Study of Majority Voting in Director Elections (November 12, 2007). Available at: https://ssrn.com/abstract=2475122.

prudence and loyalty obligations,[8] while at the same time allow them to blindly follow corporate directors in deciding what is in the best interest of the fiduciaries' plan participants.[9] Trust in management does not seem to be not an effective due diligence methodology.

Only Vote on "Corporate Events"

Mergers and acquisition transactions, dissolutions, conversions, consolidations, corporate repurchases of shares (buy-backs), issuances of additional securities with dilutive effects on shareholders, and contested elections for directors are not the only matters that may have an economic impact on a plan's investments. One example of the many other matters that may have economic impact is the vote to approve auditors. The Department points out a conflict of interest for proxy voting advisory businesses by referencing a similar paradigm with auditors. Sarbanes-Oxley mandated the independence of auditors in part by prohibiting a public accounting firm that performs an audit from simultaneously offering non-audit services.[10]

In fact, a vote against approving auditors where the firm is collecting an excessive amount of its fees from non-audit work would seem to be consistent with a fiduciary's duties to a plan. Under the second permitted practice, ERISA plans would simply not vote on auditors.

Refrain from Voting Unless a Quantitative Threshold is Met

The third permitted practice is perhaps the most concerning. In order to avoid potentially violating their obligations under section 404(a) of ERISA, plans rarely hold concentrated positions in U.S. public equities. A limitation on voting proxies based on the plan's percentage ownership in the issuer or the issuer's percentage composition within the portfolio would likely result in a silencing across most, if not all, ERISA plans. Market concentration among the largest three passive investment managers would make them the only likely candidates to vote on proxies for U.S. publicly traded companies if the standard became only those investors with a five percent stake or above should vote.[11] We do not believe the Department would advocate for only a small subset of money management industry to control the ability to communicate with corporate management and to make decisions that will impact ERISA plan investment performance.

Lastly, the Department indicates plans may be able to vote when they are the tie-breaking proxy vote or where a company needs a quorum. However, plans are unable to monitor these

[8] Proposed Rule. page 55223, see: " "Similarly, any ERISA plan fiduciary that uses a proxy advisory firm is responsible for ensuring that the proxy advisory firm's practices with respect its services to the ERISA plan are consistent with the prudence and loyalty obligations that govern the fiduciary's proxy voting actions."

[9] Ibid. page 55225. "Under this permitted practice, a fiduciary may, consistent with its obligations set forth in ERISA section 404(a)(1)(A) and (B), maintain a proxy voting policy that relies on the fiduciary duties that officers and directors owe to a corporation based on state corporate laws."

[10] Ibid. **Footnote 55:** See, e.g., GAO Report 07-765, *Issues Relating to Firms That Advise Institutional Investors on Proxy Voting* (June 2007), at 4, 9-10. By contrast, section 201 of the Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, mandates the independence of auditors in part by prohibiting a public accounting firm that performs an audit from simultaneously offering non-audit services.

[11] Walker, Owen, "Blackrock, Vanguard and SSGA tighten hold on US boards," *Financial Times,* June 15, 2019, available at: https://www.ft.com/content/046ec082-d713-3015-beaf-c7fa42f3484a.

See also: McLaughlin, David and Massa, Annie, "The Hidden Dangers of the Great Index Fund Takeover," *Bloomberg Businessweek,* January 9, 2020, available at: https://www.bloomberg.com/news/features/2020-01-09/the-hidden-dangers-of-the-great-index-fund-takeover.

conditions without incurring all the costs associated with voting in the first place.[12] Fiduciaries would not know when their shares would break a tie as that depends on the voting practices of the company's other shareholders. Similarly, fiduciaries would not know when their shares are needed to reach quorum in advance. Instead, they presumably would react when contacted by a company and may not have the systems in place to quickly research and cast a vote.

Conclusion

Engaged investors act as checks and balances, increase standards and transparency and ultimately can improve company performance, and ultimately enhance value to ERISA plan investments. Active stewardship constitutes a fundamental duty embedded in prudence and fiduciary standards. We therefore urge the Department to not adopt the Proposed Rule, which will likely silence the majority of ERISA plan investors in proxy voting. Segal Marco appreciates the opportunity to provide input on this important issue. Please contact me with any questions at 212-251-5262 or jdemairo@segalmarco.com.

Best regards,

John DeMairo

John DeMairo
President & CEO

[12] Proposed Rule, page 55226. "For example, a fiduciary declining to submit any proxy votes for holdings below a prudently determined quantitative materiality threshold may modify the policy in advance to allow proxy voting if needed for the portfolio holding to achieve a quorum or its shareholders' meeting." Also see: "Plans could also fashion policies or exceptions from policies to account for circumstances where a plan's vote share is more likely to affect the outcome of a vote and the fiduciary believes changing the outcome would have an economic impact on the plan."