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Submitted Electronically

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Jeanne Klinefelter Wilson
Acting Assistant Secretary
Employee Benefit Security Administration
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Re: Fiduciary Duties Regarding Proxy Voting and Shareholder Rights (RIN 1210-AB91)

Dear Acting Assistant Secretary Wilson:

We write on behalf of a group of clients that provides a broad range of investment and administrative services to retirement plans and investment funds subject to the Employee Retirement Income Security Act of 1974, as amended ("ERISA") (collectively, the "Group"). The Group wishes to submit comments on the Department of Labor's (the "Department's") proposed rule "Fiduciary Duties Regarding Proxy Voting and Shareholder Rights." 85 Fed. Reg. 55219 (Sept. 4, 2020) (the "Proposed Rule" or "Proposal"). Group members are involved in a variety of processes related to proxy voting, including forwarding proxy voting proposals to plan fiduciaries, administering proxy votes, evaluating recommendations provided by advisory forms, and making proxy voting decisions on behalf of a single plan or collective fund.

We appreciate the Department's efforts to comply with Executive Order 13868's (the "Executive Order") directive to review the Department's existing proxy voting guidance and determine whether it should be modified in order to "promote long-term growth and maximize return on ERISA plan assets." Executive Order 13868, 84 Fed. Reg. 15495, 15497 (Apr. 15, 2019). Nonetheless, we believe that the Proposed Rule, as drafted, will significantly increase total compliance costs associated with managing proxy voting and other shareholder proposals on behalf of ERISA-covered investors. Group members are aware of the Department's previous pronouncements addressing a fiduciary's obligations in connection with proxy voting. Heretofore, the Department's guidance has been principles-based, making clear that fiduciaries have an obligation to consider only those factors that affect the value of the plan's investment, taking into account related costs, when making proxy voting decisions. The current Proposal takes a markedly different approach, outlining a detailed, multi-step analysis and procedure that must be undertaken for each and every voting decision.

The fiduciary issues addressed by the regulation are not new and have been addressed by several administrations over the last 30 years. Each administration has interpreted proxy voting and shareholder activism fiduciary issues through its own political lens. This regulation is not required in order to interpret a new law, solve a novel problem, or address clear plan losses identified by the Department. In this regard, the Department's economic analysis fails to identify any concrete, quantifiable costs incurred by ERISA plans based solely on their proxy voting activities. As an initial comment, we ask the Department to refrain from rushing to issue a final regulation. We urge the Department to carefully consider the waterfront of comments it receives from all members of the regulated community, as well as information regarding the economic impacts and burdens of the regulation, before issuing a rule that could create more harm than good.

In addition, we submit the following specific comments to assist the Department in developing a final rule more consistent with the Executive Order's directive to maximize plan returns by reducing proxy voting compliance burdens and expenses.

1. **Revise the "Permitted Practices" so that each is a Safe Harbor**

DOL should draft the final rule so that the so-called "permitted practices" operate as safe harbors that clearly limit a voting fiduciary's liability in connection with proxy voting decisions. In the preamble to the Proposal, the Department described its rationale for developing the "permitted practices." It stated that the permitted plan policies were intended to "assist plan fiduciaries" by reducing the plan's burdens associated with analyzing proxy voting decisions that are unlikely to have an economic impact on the plan. Nonetheless, as proposed, the "permitted practices" do not clearly operate to limit a voting fiduciary's liability. Instead, the permitted practices are introduced with language that simply states that plans "may adopt" certain permitted voting policies.

It is helpful that the Proposal states in subsection (e)(3)(v) that no "permitted policy" adopted by a plan fiduciary will impose liability when the fiduciary votes (or does not vote) contrary to the policy based on whether the specific vote is expected to have an economic impact on the plan. However, as drafted, the relief provided by this provision does not provide meaningful fiduciary relief such as would be provided by a safe harbor. Moreover, the subsection's reference to the fact that a "permitted policy" shall not "preclude" fiduciary liability raises doubt as to whether compliance with "permitted policies" provides any liability relief at all.

The final rule should unequivocally state that a fiduciary will satisfy the fiduciary requirements of ERISA section 404 when it votes proxies or other shareholder proposals in compliance with the policies described under the final rule. Without a clear and effective safe harbor, a plan fiduciary will still be required to perform each step of the detailed economic analysis required by the rule regardless of the plan's voting policies, which will dramatically increase proxy voting expenses. Moreover, the Department's economic analysis of the rule's potential impact on plans as well as asset managers is entirely based on the premise that the "permitted practices" substantially eliminate or reduce plan costs. See 85 Fed. Reg. at 55232 ("The Department believes that the incremental costs of these provisions will be small on a per plan basis because the Department anticipates that most, if not all plans, will adopt policies that utilize the permitted practices…."). As written, the Department's economic analysis greatly underestimates compliance costs given that no meaningful fiduciary relief is in fact available under the permitted practices. A clear safe harbor is essential to achieving the Department's goal of reducing the burdens associated with analyzing each and every proxy vote.

2. Voting Fiduciaries will not Know when Quorum may be Impacted by the Plan's Vote

As a corollary to the Group's comment #1 above, there are two comments made by the Department in its preamble discussion of "permitted practices" that the Group believes merit specific comment. First, the preamble to the Proposed Rule's discussion of "permitted practices" references overriding or changing a plan's proxy voting policy when necessary to enable a portfolio company to achieve a quorum. See 85 Fed. Reg. at 55226. A footnote to this discussion suggests that the DOL is concerned about the negative economic impact of the company's failure to obtain a quorum on the value of the plan's investment. The Department's reference to amending the plan's proxy voting policy when necessary to support a quorum completely ignores the fact that plans will never know when their vote alone will impact a quorum. And, more to the point, all shareholder votes impact a company's ability to obtain a quorum—a fundamental fact that weighs in favor of permitting ERISA plans to vote proxies under more flexible principles-based rules such as those that exist under current guidance.

More importantly, this example makes clear that the permitted practices as proposed by the Department are not safe harbors and do not provide meaningful liability relief. The example shows that, at least in the view of the Department, a plan fiduciary or investment manager might have to consider other potential costs to the issuer as having a negative economic impact on the value of the plan's investment and might have to override or amend its policy on a vote-by-vote basis. However, neither the Proposal nor the preamble give examples of how a voting fiduciary might be required to consider or quantify such costs.

The second example that the Group believes merits comment concerns the Department's statement that a plan could adopt of policy of not voting on non-binding proposals, unless it is aware that such proposal will have an economic impact on the value of the plan's investment. Group members are struggling to understand whether a non-binding proposal could ever have an economic impact on the plan's investment. Again, this statement suggests that a fiduciary cannot follow its voting policy without, in each case, performing additional analysis to be sure that each voting decision will satisfy ERISA.

These examples illustrate why Group members believe that the rule as proposed will ultimately greatly increase proxy voting compliance costs rather than ease them. The Group again urges the Department to issue a final rule that includes fiduciary liability relief in the form of safe harbors for voting decisions made in compliance with permitted proxy voting policies. Without safe harbors, the rule only complicates voting decisionmaking.

3. **The Regulation does not take into account the Limited Perspective of an Investment Manager**

The economic analysis required to be performed under the Proposed Rule ignores the fact that the vast majority shares of publicly traded company stock held by ERISA plans are managed by professional investment managers meeting the requirements of ERISA section 3(38), either in the context of separately managed accounts, pooled insurance company separate accounts or collective investment trusts. Most plan sponsors delegate management authority to these managers, including the authority to vote proxies. The threshold economic determination required under the Proposal would require such a manager to "consider the likely impact on the investment performance *of the plan* based on such factors as the size of the *plan's* holdings in the issuer relative to the total investment assets of the *plan*" and "the *plan's* percentage ownership of the issuer." See Proposed Rule, subsection (e)(2)(ii)(B) (emphasis added). Moreover, the manager would be required to vote where the vote would have an economic impact on the *plan*, and abstain from voting unless the fiduciary determines that the vote would have an economic impact on the *plan*. See Proposed Rule, subsection (e)(3) (emphasis added). These rules clearly contemplate an analysis that focuses solely on the economic impact of the vote on an individual ERISA *plan's* portfolio as a whole (taking costs into account).

This required analysis will be impossible for an investment manager to perform in the vast majority of cases. Even in the context of a single customer account, an investment manager will have visibility only into the slice of the plan's portfolio managed by the manager. The manager will not know whether and how many shares of the issuer are contemporaneously held in other portions of the plan's portfolio, and will not know the percentage of the issuer that the plan's portfolio owns in total. Information regarding the total number and value of shares of any single issuer held on a plan-wide basis will be known, if at all, only by the plan's trustee or named fiduciary, not an investment manager.

Moreover, the Department's economic analysis supporting the Proposal does not take into account the costs that investment managers will incur in creating new proxy voting and monitoring systems to comply with each plan client's proxy voting procedures, which will be substantial.

The final rule should clarify that an investment manager that has been delegated voting authority is responsible for performing the required economic analysis taking into account only the portion of the plan's portfolio managed by the manager.

4. <u>The Rule Will Silence ERISA Plan Investors where Voting may be Economically Appropriate</u>

As we explained in comment #3 above, the economic analysis required by the Proposed Rule is focused on analyzing whether the vote at issue will have an economic impact on <u>a single plan's portfolio</u> as a whole, based on the plan's percentage of ownership in the company and the portion of the plan's total portfolio represented by the stock. <u>See</u> <u>Proposed Rule</u>, subsection (e)(2)(ii)(B). Further, the Proposal requires the voting fiduciary to abstain from voting unless the voting fiduciary determines that the matter being voted upon would have an economic impact on the plan's portfolio as a whole. <u>See</u> <u>Proposed Rule</u>, subsection (e)(3).

This required analysis, focused on anticipated economic impacts on a single plan, ignores the fact that several related plans may together own a significant stake in a company. Where several related plans, such as in the context of related multiemployer plans, together own a large share of a company, all plans voting together could create an economic impact on each individual plan's investment performance such that voting may be appropriate. The analysis also ignores the fact that a single 3(38) investment manager may exercise voting authority over several unrelated ERISA, non-ERISA and pooled investment fund accounts that together own a significant stake in a company. This could easily be the case where a manager has a proven expertise in a certain specific strategy or market sector. Such a manager could manage a significant stake in a given company on behalf of many clients under circumstances where any single ERISA investor's share of the company is deminimis. We believe that the rule will have an unwarranted chilling effect on votes exercised by ERISA plans under circumstances where many ERISA and non-ERISA investors, voting together, could impact the economics of the investment and, as a result, each investors' portfolio.

The Proposal's strong prejudice against permitting ERISA plans to vote will, in effect and over time, silence ERISA plan votes. Under current guidance, the Department has made clear that ERISA plan investors have a fiduciary obligation under ERISA to vote proxies on issues that may have an economic impact on the plan's investment, considering the costs involved. <u>See</u> Interpretive Bulletin 2016-01, 29 C.F.R. § 2509.2016-01. The Group believes that an unintended consequence of the Proposal is that non-ERISA voters will always control voting outcomes, and these non-ERISA voters may analyze and cast votes based on any number of non-economic factors. The Group believes that the Department's Proposal will, in effect, prohibit voting by a sector of shareholders that are legally obligated to vote solely in the economic interests of the investment. Under certain circumstances, voting together, many

ERISA shareholders could have an economic impact on the value of each plan's investment in the company. The Group believes that, over time, the Proposed Rule could erode the value of plan investments by prohibiting ERISA plans from voting on most matters.

5. **The Monitoring Obligation Described by the Rule is Unreasonable**

It is well established that when a plan fiduciary hires a service provider, ERISA requires the fiduciary to monitor the services provided to make sure that the services remain appropriate for the plan, high in quality, cost effective, and solely in the interest of the plan and its participants. See 29 C.F.R. 2509.75-8, Q-17; DOL Field Assistance Bulletin 2002-3 (Nov. 5, 2002). Nonetheless, the Department has never required a hiring fiduciary to second-guess a professional service provider, or to re-perform every act that the provider performs for the plan.

The Proposed Rule recognizes that it is common for a plan fiduciary to delegate proxy voting authority to a 3(38) investment manager hired to manage a plan portfolio. Nonetheless, the rule requires the plan fiduciary to require the manager to document each proxy voting decision made by the manager, including the rationale for each voting decision. See Proposed Rule, subsection (e)(2)(iii). The same rule applies where the plan hires a proxy voting advisory service to advise on voting proposals. Thus, the rule appears to require the hiring fiduciary to, in effect, "peer over the shoulder" of the investment manager or advisor, supervising each and every voting decision to confirm that the voting decision was made based on the economic impact on the plan.

We disagree that ERISA requires a plan fiduciary to perform such a granular level of monitoring of a professional service provider. For example, the Department has addressed how a plan fiduciary may monitor a fiduciary investment advice provider in Field Assistance Bulletin 2007-01 (Feb. 2, 2007). The Department explained that the fiduciary should monitor such factors as compliance with licensing and contractual requirements, participant utilization, fees, and changes in status that contributed to the hiring decision; however, the Department also made clear that the fiduciary is not required to monitor the specific advice provided. We believe that a named fiduciary likewise has no duty to monitor each and every proxy voting decision made by a 3(38) investment manager. This is made clear in ERISA itself. ERISA section 405(d) specifically provides that when a 3(38) investment manager has been properly appointed, no trustee or other fiduciary has the obligation to manage the assets under the manager's discretion. Thus, section 405(d) recognizes when a professional investment manager has been hired to manage the plan's assets, it is contrary to the plan's interests for any other fiduciary to duplicate each decision that the manager makes. The Group asks the Department to eliminate the requirement that a fiduciary require its managers and advisors to document each and every voting decision along with the rationale for each decision. The Group believes that the provision will create unmanageable liability risk for fiduciaries by suggesting an obligation to review every voting decision made.

6. The Required Analysis for each Proxy Vote is Excessively Burdensome

As explained by the Department, the Proposed Rule was drafted in order to address two key concerns. First, the Department wishes to clarify that ERISA does not require a fiduciary to vote each and every proxy or other shareholder proposal that arises from the plan's portfolio. Second, the Department is concerned that undue resources have been wasted on proxy voting activities that have no impact on the plan's economics. Nonetheless, as drafted in its current form, the rigorous, multi-step analysis required by the Proposal would apply to each and every individual vote that comes before the plan's fiduciary, particularly in light of the fact that no meaningful liability relief is available in connection with the Proposal's permitted practices.

Based on our review of the Proposal, for each and every vote, the voting fiduciary would be required to perform--at a minimum--each of the following steps:

(1) Analyze whether the vote will impact the investment performance of the plan as a whole, based on the size of the plan's holding in the issuer relative to the plan's total portfolio, and the plan's percentage ownership of the issuer;
(2) Ensure that the vote does not subordinate the interests of the plan's participants and beneficiaries to non-pecuniary objectives, or sacrifice risk or return to promote non-pecuniary goals;
(3) Research the materials facts surrounding the vote and issuer;
(4) Not rely on advice provided by a professional proxy advisory service without extensive review and approval of the advisor's policies;
(5) Consider the costs of voting and researching the vote, and whether such costs impact the economic analysis of the vote;
(6) Cast a vote where it is determined that the vote would have an economic impact on the plan as a whole;
(7) Abstain from voting unless the vote is determined to have an economic impact on the plan as a whole; and
(8) Document the voting decision, including the basis for each voting decision

Failure to satisfy each one of the above requirements will put the plan's fiduciary at risk of liability for a fiduciary breach. This is a far more nuanced and particularized series of obligations than the Department has ever articulated in connection with proxy voting. And, given that following the Department's "permitted practices" do not yield meaningful relief from fiduciary liability, the Group believes that the Department's economic analysis substantially underestimates the compliance costs attendant to establishing and implementing these procedures. Thus, while the Proposal appears to have been designed to ease proxy voting burdens and reduce related expenses, as drafted, the Proposal will have the opposite effect. Plan expenses related to proxy voting compliance will substantially increase.

7. The Department's Analysis does not Acknowledge that Investment Advisers must comply with Different Standards under SEC Guidance

On its face, the Department's Proposed Rule is inconsistent with the SEC's guidance on proxy voting, and registered investment advisers ("RIAs") will have to navigate conflicting duties under the Investment Advisers Act of 1940 (the "Adviser's Act") and the Proposal. For example, SEC guidance generally requires investment advisers to vote proxies unless the adviser determines it is in the client's best interest to not vote. See Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, 84 Fed. Reg. 47420 (Sept. 10, 2019). Thus, the SEC guidance generally favors voting in most instances consistent with the adviser's fiduciary duties to its clients. Yet the Department's Proposal would affirmatively prohibit an adviser from voting unless the adviser prudently determines the vote would yield an economic impact on the ERISA's investor's portfolio as a whole. Thus, the Department's Proposal imposes a different legal standard that strongly disfavors voting. Thus, RIAs that manage accounts for both ERISA and non-ERISA clients will be subject to meaningfully different voting standards and will have to implement different voting processes across the ERISA and non-ERISA client base. The Department's economic analysis justifying its Proposal fails to acknowledge the significant burdens and costs this will impose on asset managers as they attempt to develop systems to comply with conflicting legal regimes. For this reason, the Group urges the Department to allow registered investment advisors to satisfy ERISA by satisfying their proxy voting obligations under the Adviser's Act. At a minimum, the Department must factor into a revised economic analysis the significant costs RIAs will face as they attempt to come into compliance with conflicting legal standards.

8. Clarify that the Rule does not apply to the Voting of Mutual Fund shares held by ERISA Plans

In its economic analysis, DOL made clear that the Proposed Rule does not apply to the voting of shares of registered investment companies held by ERISA plans. See 85 Fed. Reg. at 55237 ("Plans that only hold their assets in registered investment companies, such as mutual funds, will be unaffected by the proposed rule."). Based on our conversations with Group members and other clients, we believe there is substantial misunderstanding within the retirement plan community as to the scope of the rule.

ERISA plan customers receive a variety of proxies that must be evaluated on a daily basis, not only in connection with shares of common stock held by the plan, but also from registered investment companies, bank collective trust funds and other collective funds in which the plan invests. The regulated community needs to be able to clearly identify those proxies that are subject to the requirements of the Proposal and those that are not. We ask the Department to set forth in the rule itself, rather than in the preamble or economic analysis, that plan investments in registered investment companies, bank collective funds and other securities are not subject to the requirements of the rule. Such a clarification will avoid confusion and go a long way toward reducing compliance burdens.

9. <u>Clarify that Participant Voting is not subject to the Rule</u>

The Department should clarify that the Proposal's requirements do not apply to participants who vote shares of stock held in their ERISA-covered plan accounts. For example, many ERISA-covered 401(k) plans offer self-directed brokerage windows through which participants can invest in publicly traded companies as well as registered investment companies and many other securities. These self-directed brokerage windows invariably involve the broker passing proxy voting rights through to the participants who hold the securities through their plan accounts. Moreover, many participant directed ERISA-covered plans allow participants to invest in company stock in a company stock fund. In order to qualify for the limited fiduciary liability available under ERISA section 404(c)(1) and applicable Department regulations, these plans are required to pass voting rights appurtenant to the shares through to participants who hold the shares through the plan. It is true that ERISA section 404(c)(1)(A)(i) provides generally that plan participants are not fiduciaries; however, many ERISA-covered plans have been drafted to explicitly provide that plan participants are deemed "named fiduciaries" when they vote securities held by their plan accounts. This approach is based on long-standing guidance from the DOL that permits the plan's trustee to enjoy the limited liability available under ERISA section 403(a)(1) where the trustee is directed by a "named fiduciary." <u>See</u> DOL Letter to Thobin Elrod (Feb. 23, 1989). DOL should clarify that the requirements of the Proposed Rule do not apply to participants when they exercise voting rights related to securities held in their plan accounts, even if the plan deems them "named fiduciaries."

10. <u>The Proposed Rule Contains Overly Prescriptive Rules</u>

The Proposed Rule would require fiduciaries to review proxy voting policies at least once every two years. The Department's justification for this interval is that it understands this is "consistent with industry practices…." 75 Fed. Reg. at 55226. The Department also requested comment on whether a five-percent ownership threshold could be used for measuring the percentage of the plan's total portfolio below which a plan fiduciary would not vote any proxy.

The Group is concerned that the Department would interpret ERISA's prudence requirement as imposing an absolute requirement on a plan fiduciary to review the plan's proxy voting policies every two years. The Department usually refrains from specifying absolute rules, viewing prudence as judged based on the specific facts and circumstances of individual cases.

The Group is concerned that such a clear rule will create potential liability for fiduciaries in their ongoing monitoring of other plan policies, such as investment policy statements, fiduciary charters, plan expenses and other policies, or in connection with the frequency of RFPs. The Group asks the Department to eliminate the two-year monitoring rule, leaving fiduciaries free to monitor such policies at an interval that makes sense in light of each plan's unique resources and priorities. In addition, the Group asks the Department avoid specifying a permitted practice that identifies a percentage cap on the portion of a plan's portfolio that must be represented by an issuer in order for proxy votes to be considered. This decision is more appropriate for individual plans and managers to make based on the specific strategy and goals of the plan or portfolio.

11. <u>The Department should adopt a longer Effective Date</u>

The Group is very concerned that the proposed 30-day effective date will not allow sufficient time to develop, communicate and implement the significant procedural changes required by the Proposed Rule. This is particularly true for asset managers who may have to implement and perform related programming for proxy voting policies across numerous ERISA and non-ERISA customers, each one of whom may develop a unique proxy voting policy. The current COVID-19 national emergency also weighs in favor of a longer period of time to come into compliance with a new and substantially changed regulatory scheme.

The Group recognizes that the Department may be reluctant to adopt a longer effective date given the possible change in administrations. For this reason, the Group requests, in the absence of a change, a non-enforcement policy to the effect that the Department will not take action against a fiduciary during the first 180 dates following the effective date, as long as the fiduciary can demonstrate a good faith effort to come into compliance with the new rule.

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We hope these comments are helpful to the Department in drafting a final rule that will result in reduced proxy voting compliance costs and thus higher returns for ERISA plans, participants and beneficiaries. We would be happy to discuss our comments with the Department in a socially distant meeting or teleconference if that would be helpful.

Respectfully submitted,

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