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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: *Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights*; RIN 1210-AC03

Dear Acting Assistant Secretary Khawar:

Thank you for the opportunity to comment on “*Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights*,” the proposed rules recently issued by the Employee Benefits Security Administration of the Department of Labor (“DOL”).

Glass, Lewis & Co., LLC (“Glass Lewis”) applauds DOL for revisiting the amendments made late in the last Administration to ERISA’s investment duties regulation and strongly supports the proposed changes. Glass Lewis’ primary business consists of providing research and advice to investors, including retirement plan fiduciaries, to enable them to effectively and efficiently make and execute proxy voting decisions. As such, we appreciate the importance of retirement plan fiduciaries’ managing plan assets, including voting and other shareholder rights, in the best interest of their plan participants.

Regrettably, however, the political origins, rushed process and substance of the rules adopted last year suggest that they were not a genuine effort to advance the interests of plan participants. Instead, they seemed to be a concession to certain companies that wished to curtail investors’ considerations of ESG factors and to bias them against exercising their basic rights as shareholders. The proposed changes would eliminate the unwarranted skepticism of ESG considerations and proxy voting that pervaded the last rulemaking and free up fiduciaries to again act in the best interest of their plan participants. We encourage DOL to adopt the proposed changes expeditiously.

## I. Background

### A. Glass Lewis

Founded in 2003, Glass Lewis is a leading independent proxy advisor. As a proxy advisor, Glass Lewis provides proxy research and vote management services to institutional investor clients throughout the



world. While, for the most part, investor clients use Glass Lewis research to help them make proxy voting decisions, these institutions also use Glass Lewis research when engaging with companies before and after shareholder meetings. Further, through Glass Lewis' web-based vote management system, Viewpoint, Glass Lewis provides investor clients with the means to receive, reconcile, and vote ballots according to custom voting guidelines and record-keep, audit, report, and disclose their proxy votes.

Glass Lewis serves more than 1,300 institutional investor clients -- primarily public pension funds, mutual funds and other institutions that invest on behalf of individual investors and have a fiduciary duty to act, including through proxy voting, in the best interests of their beneficiaries. In 2020, Glass Lewis issued over 27,000 proxy research reports on over 21,000 companies headquartered in 87 countries around the globe.

A significant majority of Glass Lewis' clients today have their own custom voting policies. Glass Lewis helps these clients implement their policies by applying them to the circumstances presented by companies in their proxy statements and recommending how they vote accordingly. During the policy formulation process, an institution will review Glass Lewis' policies to assess the similarities and differences between the institution's views and Glass Lewis' "house policy." Glass Lewis engages extensively with institutional investors and aims to have policies that reflect the views of its clients. Accordingly, it is not uncommon for an investor client to elect to implement the same policy as Glass Lewis for some of the issues up for vote. Some Glass Lewis customers employ hybrid policies. Vote decisions of hybrid policy clients may be based on a combination of recommendations generated by the client custom policy, the Glass Lewis house policy, and issues that were "referred" for case-by-case analysis by the customer.

Glass Lewis also executes votes on behalf of investor clients in accordance with the specific instructions of those clients. Whether customers elect to receive vote recommendations according to a custom policy, a hybrid policy, or the Glass Lewis house policy, they control when and how votes are cast. To that end, Glass Lewis implements client voting policies on its vote management system so that each ballot populates with recommendations based on the specific policies of the client, enabling the client to submit votes in a timely and efficient manner. (Under no circumstance is Glass Lewis authorized to deviate from a client's instructions or to determine a vote that is not consistent with the policy specified by the client.) When a preliminary ballot is ready for review, the voting system will alert the client and provide such client with relevant disclosures and other information needed to review and evaluate the matters up for a vote. Clients can choose to restrict the submission of a ballot until after their authorized personnel have reviewed and approved the votes. Clients can also make — and often do make — changes to their preliminary ballots before signing off. And, assuming the voting deadline has not passed, they can even change their votes and resubmit them. Customers are responsible for designing and managing their vote management preferences, as well as assigning review and voting rights to users. Glass Lewis is responsible for ensuring that voting is conducted in accordance with customer instructions.



## B. The Role of Proxy Advisors

Glass Lewis believes that proxy advisors play an important support role, providing resources and technical, subject-matter expertise to help institutional investors meet their fiduciary responsibility to vote securities on behalf of their participants and beneficiaries in a cost-effective way. As the U.S. Securities and Exchange Commission (“SEC”) has explained, “When making voting determinations on behalf of clients, many investment advisers retain proxy advisory firms to perform a variety of functions and services.... Contracting with proxy advisory firms to provide these types of functions and services can reduce burdens for investment advisers (and potentially reduce costs for their clients) as compared to conducting them in-house.”<sup>1</sup>

As an increasing share of investors own stock indirectly, such as through mutual and pension funds, these individual investors are dependent on those institutional investors to vote on their behalf and act in their best interest. In order to do so both effectively and efficiently, those institutional investors often leverage their resources by using the services of a proxy advisor. As the Council of Institutional Investors and a coalition of investors have explained:

Retail holders now invest much of their capital with institutional investors because they understand that institutional investors’ expertise and size bear the expectation of higher returns, lower costs and mitigated risks. Importantly, retail investors also understand that aggregating their individual holdings into larger, concentrated blocks through an institutional manager allows for more effective monitoring of company management.

Even so, institutional investors themselves face challenges in spending significant time and resources on voting decisions because the funds and other vehicles they manage receive only a portion of the benefits conveyed on all investors of the relevant enterprise.

Proxy advisors are a market-based solution to address many of these practical cost issues. Proxy advisors effectively serve as collective research providers for large numbers of institutional investors, providing these investors an affordable alternative to the high costs of individually performing the requisite analysis for literally hundreds of thousands of ballot proposals at thousands of shareholder meetings each proxy season.<sup>2</sup>

In addition, proxy advisors provide a viable solution for asset managers and other investors seeking a way to mitigate their own conflicts of interest when voting shares on behalf of their participants or beneficiaries. As the SEC has noted, an investment adviser “may look to the voting recommendations of a proxy advisory firm when the investment adviser has a conflict of interest, such as if, for example, the investment adviser’s interests in an issuer or voting matter differ from those of some or all of its

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<sup>1</sup> U.S. Securities and Exchange Commission, Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, Release No. IA-5325 at 5 (Aug. 21, 2019) (“SEC August 2019 Guidance”).

<sup>2</sup> Letter of Ken Bertsch, Executive Director, Council of Institutional Investors and 60 institutional investors to Former SEC Chairman Jay Clayton, at 2 (Oct. 15, 2019), available at [https://www.cii.org/files/issues\\_and\\_advocacy/correspondence/2019/201910015proxy\\_advisor\\_sign\\_on\\_final.pdf](https://www.cii.org/files/issues_and_advocacy/correspondence/2019/201910015proxy_advisor_sign_on_final.pdf).



clients.”<sup>3</sup> While the ultimate responsibility of voting proxies in the best interest of its clients continues to lie with the investment adviser, the SEC has signaled that “this third-party input into such an investment adviser’s voting decision may mitigate the investment adviser’s potential conflict of interest.”<sup>4</sup>

## II. Analysis of the Proposed Rules

### A. Proxy Voting and Exercise of Shareholder Rights

The rules adopted by DOL in 2020 on proxy voting and the exercise of shareholder rights were the result of a flawed regulatory process and risk depriving plan participants of the benefits of shareholder engagement. DOL should remove the bias and prescriptiveness of the 2020 rules and reaffirm the balanced approach in its prior proxy voting guidance by adopting the four changes proposed and making one other change to the current rules.

#### The Deficient Process of the 2020 Rulemakings

We appreciate that agencies do not often or lightly revisit their past rulemakings, even where, as here, those rules have not fully gone into effect and no significant reliance interests are at stake. Here, however, that institutional reluctance should play no role. Rather than a genuine effort to seek public comment and come to a sound and reasoned interpretation of ERISA that advances the interests of plan participants, the investment duties regulation adopted last year was instead a rushed, predetermined and politicized misuse of the regulatory process to entrench the preferred investor and shareholder behavior of certain companies into a DOL rule. Among other things --

- The origin of the rulemakings was an Executive Order, which was not intended to protect retirement plan participants, but to “promote private investment” in certain companies with adverse ESG profiles;<sup>5</sup>
- Even though both rulemakings resulted in the first ERISA regulations on the subject and OMB designated each of them a “major rule,” both proposals were only exposed for comment for 30 days, half the time that is generally recognized as the minimum for the public to have a meaningful opportunity to comment on proposed rules;<sup>6</sup>

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<sup>3</sup>SEC August 2019 Guidance at 5-6.

<sup>4</sup> Id.

<sup>5</sup> Executive Order No. 13,868, 84 FR 15495, Promoting Energy Infrastructure and Economic Growth (Apr. 10, 2019) (directing DOL to determine whether existing guidance on the fiduciary responsibilities for proxy voting should be rescinded, replaced, or modified in order to “promote private investment in the Nation’s energy infrastructure”).

<sup>6</sup> Executive Order No. 12,866, Regulatory Planning and Review, 58 FR 51735 (Oct. 4, 1993) (“In addition, each agency should afford the public a meaningful opportunity to comment on any proposed regulation, which in most cases should include a comment period of not less than 60 days.”).



- Even though the proxy voting proposal involved myriad, important changes to DOL's then current guidance, those changes were not even acknowledged, let alone explained and justified, in DOL's preamble to the proposed rules;<sup>7</sup>
- The proxy voting regulatory impact analysis was based on what DOL called an "illustration." Compounding its failure to rely on any real data or evidence, the model used in this illustration was deeply flawed and therefore led to wildly-overstated assumptions about the cost of proxy voting;<sup>8</sup> and
- The final proxy voting rules were issued only two months after the comment period ended (and only five weeks before the transition to a new Administration), with little discussion of the points made in the numerous comment letters opposing the proposal and little, if any, explanation of key elements of the final rules.

Given these procedural infirmities, DOL is to be commended for reopening the rulemaking process and should not hesitate to reach its own determination, after conducting a new and reasoned deliberative process, of what is in the best interest of plan participants and beneficiaries.

## DOL's Proposed Changes

DOL proposes to remove four specific aspects of the 2020 rules that added burdens and sought to discourage ERISA fiduciaries from responsible stewardship activities. For the reasons below, Glass Lewis strongly supports each of the changes and urges their adoption.

### i. Eliminating language discouraging proxy voting.

First, DOL proposes to eliminate the statement added to the rule in 2020 that "[t]he fiduciary duty to manage shareholder rights appurtenant to shares of stock does not require the voting of every proxy or the exercise of every shareholder right." This statement is both unnecessary and, in concert with the other 2020 rule changes and preamble discussion, misleadingly signaled to fiduciaries that proxy voting is costly and unimportant. We support its deletion from the rule.

This statement was purportedly added to the rules to prevent a "persistent misunderstanding" that ERISA fiduciaries must always vote proxies. But, as Glass Lewis explained in its comment letter on the 2020 rules, DOL's "evidence" of this supposed misunderstanding primarily consisted of a few assertions to that effect by management trade associations and their lawyers. DOL itself has clearly told fiduciaries they do not need to vote all proxies in its prior guidance and DOL provided no evidence from its industry oversight that ERISA fiduciaries are, in fact, voting all proxies out of some mistaken belief. Our experience is that plans and their asset managers recognize they do not need to vote when the costs of

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<sup>7</sup> See Letter of Kevin Cameron and Nichol Garzon-Michell, Glass Lewis, to DOL at 12-14 (October 5, 2020) (delineating all the changes that would be made without any acknowledgement or DOL explanation for them) ("Glass Lewis Comment Letter") (attached); see also *Encino Motorcars, LLC v. Navarro*, 136 S.Ct. 2117, 2125-26 (2016) (agency "must at least display awareness that it is changing position and show that there are good reasons for the new policy") (internal quotations omitted).

<sup>8</sup> See Glass Lewis Comment Letter at 24-28.



doing so exceed its expected benefits, such as in certain situations involving foreign securities. This is no less true of other exercises of shareholder rights.

In addition to being unnecessary, the 2020 amendment was potentially misleading, particularly when read with the other 2020 rule changes and accompanying preamble discussion. As DOL now recognizes, including this statement in the rules might be understood to mean that fiduciaries should be indifferent to exercising their rights as shareholders. Avoiding this misunderstanding is particularly important, as DOL notes, “in circumstances where the cost is minimal as is typical of voting proxies.”

Glass Lewis agrees that eliminating this statement will avoid potential misunderstandings that proxy voting is unimportant and costly. As Glass Lewis also noted in its previous comment letter, fiduciaries have increasingly focused on proxy voting and shareholder engagement because it adds value, both for the individual companies in their portfolio and for the portfolio as a whole. Shareholder votes on the election of directors (which constitute a majority of proxy votes) convey important information about shareholders’ views and can and do affect companies’ decisions about who should serve as corporate directors.<sup>9</sup> Active ownership can produce significant financial benefits to a retirement plan’s participants.<sup>10</sup>

DOL’s 2020 rules also ignored the important role of shareholder engagement in risk mitigation. DOL’s own prior proxy voting guidance had recognized that the “financial crisis of 2008 exposed some of the pitfalls of shareholder inattention to corporate governance and highlighted the merits of shareholders taking a more engaged role with the companies.”<sup>11</sup> And emerging academic research shows that shareholder attention to ESG issues can significantly reduce investment risk.<sup>12</sup> None of this was discussed or reconciled with the 2020 rules’ repeated suggestions that proxy voting and engagement do not add value and are only being carried out to further managers’ political preferences or out of a mistaken belief they are required. As the regulatory preamble to its proposed rule changes correctly notes, the “exercise of shareholder rights is important to ensuring management accountability to the shareholders that own the company.... In general, fiduciaries should take their rights as shareholders seriously, and conscientiously exercise those rights to protect the interests of plan participants.”

It is also important for DOL to correct the repeated suggestions in the 2020 rulemaking that fiduciaries should opt out of voting to save costs. For example, in proposing its 2020 rules, DOL professed, with no

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<sup>9</sup> See for example Yaron Nili & Kobi Kastiel, *Competing for Votes*, 10 Harv. Bus. L. Rev. 287 (2020) (“Shareholder voting matters. It can directly shape a corporation’s governance, operational and social policies. But voting by shareholders serves another important function—it produces a marketplace for votes where management and dissidents compete for the votes of the shareholder base. The competition over shareholder votes generates ex ante incentives for management to perform better, to disclose information to shareholders in advance, and to engage with large institutional investors.”), available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3681541](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3681541).

<sup>10</sup> Letter from Jon Lukomnik, Keith Johnson et al. to the Department of Labor on the Proposed ESG Rule (July 21, 2020) (“Lukomnik Letter”), available at <https://corpgov.law.harvard.edu/2020/07/21/comment-letter-on-proposed-regulation-of-esg-standards-in-erisa-plans/>.

<sup>11</sup> Interpretive Bulletin 2016-01, 81 Fed. Reg. 95,879, at 9 (Dec. 29, 2016) (“2016 Interpretive Bulletin”).

<sup>12</sup> Hoepner, Andreas G. F., Ioannis Oikonomou, Zacharias Sautner, Laura T. Starks and Xiaoyan Zhou, “ESG Shareholder Engagement and Downside Risk,” AFA 2018 paper (Aug. 10, 2018), available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2874252](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2874252).



cited basis, to be “concerned that the costs for fiduciaries to prudently exercise proxy voting rights often will exceed any potential economic benefits to a plan.” But DOL never tried to reconcile this professed concern with its prior recognition that “[i]n most cases, proxy voting and other shareholder engagement does not involve a significant expenditure of funds by individual plan investors.”<sup>13</sup> In fact, DOL’s 2020 regulatory impact analysis vastly overstated the costs of proxy voting through the illogical and unrealistic assumption that each retirement plan would conduct all its own research and analysis of each proxy vote. As DOL previously recognized, however, most proxy voting and engagement “are engaged in by institutional investment managers [who] often engage consultants, including proxy advisory firms, in an attempt to further reduce the costs of researching proxy matters and exercising shareholder rights.”<sup>14</sup> In other words, DOL ignored basic economies of scale and efficiency that can be achieved through outsourcing aspects of stewardship.<sup>15</sup> As DOL’s current regulatory preamble correctly notes: “The solution to proxy-voting costs is not total abstention, but is, instead, for the fiduciary to be prudent in incurring expenses to make proxy decisions and, wherever possible, to rely on efficient structures (e.g., proxy voting guidelines, proxy advisers/managers that act on behalf of large aggregates of investors, etc.)”

In sum, DOL’s proposed change is an important corrective to the unbalanced emphasis on costs and minimization of the benefits of proxy voting in the 2020 rulemaking and we encourage its adoption.

## ii. Eliminating special monitoring obligations.

Next, DOL proposes to eliminate a provision in the 2020 rule that imposed a specific monitoring responsibility “[w]here the authority to vote proxies or exercise shareholder rights has been delegated to an investment manager pursuant to ERISA section 403(a)(2), or a proxy voting firm or other person who performs advisory services as to the voting of proxies.” Because it is redundant, unnecessary, and unclear, we support DOL’s proposal to eliminate this aspect of the rule.

First, this change avoids redundancy in the rule and related uncertainty for ERISA fiduciaries. As DOL notes, another part of the rule already imposes a more general duty of prudence and diligence in the

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<sup>13</sup> 2016 Interpretive Bulletin.

<sup>14</sup> See *id.* (“**In most cases, proxy voting and other shareholder engagement does not involve a significant expenditure of funds by individual plan investors** because the activities are engaged in by institutional investment managers . . . . Those investment managers often engage consultants, including proxy advisory firms, in an attempt to further reduce the costs of researching proxy matters and exercising shareholder rights. . . . **[M]any proxy votes involve very little, if any, additional expense to the individual plan shareholders to arrive at a prudent result.**”) (*emphasis added; footnote omitted*”).

<sup>15</sup> See Michael Cappucci, Harvard Management Company, “The Proxy War Against Proxy Advisors,” at 7-8 (Nov. 16, 2019) (“Importantly, [proxy advisors] economize the proxy research and voting functions by spreading the costs of tracking, analyzing, and processing many thousands of proxy votes over a larger pool of shareholders.”), available at <https://corpgov.law.harvard.edu/2019/11/27/the-proxy-war-against-proxy-advisors/>; see also comments of former SEC Chair Jay Clayton at the U.S. Chamber of Commerce event on “Corporate Governance: Making the Case for Reform” (July 16, 2019) (“Outsourcing . . . in itself is not a bad thing. All the time in America we create value through outsourcing, outsourcing ministerial tasks, in this case, of going through filings and crunching the data, providing data reports, that’s good. It probably saves shareholders, saves investors money.”), available at <https://www.centerforcapitalmarkets.com/event/corporate-governance-making-the-case-for-reform/>.





selection and monitoring of stewardship service providers. Section (d)(2)(ii)(E) of the rule requires plan fiduciaries to:

Exercise prudence and diligence in the selection and monitoring of persons, if any, selected to exercise shareholder rights or otherwise advise on or assist with exercises of shareholder rights, such as providing research and analysis, recommendations regarding proxy votes, administrative services with voting proxies, and recordkeeping and reporting services.

In our experience, ERISA fiduciaries take their existing selection and monitoring responsibilities, as long articulated in DOL guidance, seriously and codifying those responsibilities in (d)(2)(ii)(E) of the rule is appropriate and sufficient for this practice to continue.

The preamble to DOL's final 2020 rules does not explain why this provision applies to "proxy voting firm[s]."<sup>16</sup> To the extent it was meant to address some concern or risk to plan participants when an ERISA fiduciary uses the services of a proxy advisor, the existence of any such risk was never substantiated in any way as part of DOL's 2020 rulemaking. The DOL's preambles in that rulemaking were laced with the unsupported allegations of proxy advisor critics and references to "concerns" expressed to the SEC as part of its 2020 proxy advice rulemaking. For example, the 2020 proposed rules' preamble recited issuer trade associations' claims that proxy advisors have made what the preamble called "factual and/or analytic errors."

This issue, however, was thoroughly explored and debunked as part of the 2020 SEC proxy advisor rulemaking. In that rulemaking, corporate management advocacy groups expressed "concerns" about errors in proxy advice and the SEC proposed an issuer pre-review regime to "promote accuracy" in proxy advice.<sup>17</sup> The comment process in that rulemaking, however, revealed that these "concerns" were anecdotes and generalized allegations based on surveys; there simply was no evidence of a significant error rate in proxy advice. The SEC's own Investor Advisory Committee demonstrated that a chart used by the SEC in its proposal reflected that issuers only claimed proxy advice errors 0.3% of the time and "none of those [were] shown to be material or to have affected the outcome of the related vote."<sup>18</sup> Even with respect to this small number of claimed errors, an analysis by the Council of Institutional Investors revealed that "most of the claimed 'errors' actually [were] disagreements on analysis and methodologies, and that some other alleged proxy advisory firm errors derive from errors in the company proxy statements."<sup>19</sup> Tellingly, the SEC disavowed its claim of proxy advisor inaccuracy as the

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<sup>16</sup> In fact, in the preamble to the final rules, after reciting the concerns of commenters, including Glass Lewis, and questions about how and why the proposed rule applied to proxy advisors, DOL simply adopted a version of the rule without responding to those concerns and questions in any discernible way.

<sup>17</sup> U.S. Securities and Exchange Commission, Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice, Release No. 34-87457, at 110 (Nov. 5, 2019).

<sup>18</sup> See Recommendation of the SEC Investor Advisory Committee Relating to SEC Guidance and Rule Proposals on Proxy Advisors and Shareholder Proposals (Jan. 24, 2020) (emphasis in original), available at <https://www.sec.gov/comments/s7-22-19/s72219-6698769-206000.pdf>.

<sup>19</sup> Letter of Ken Bertsch, Executive Director, Council of Institutional Investors to Chairman Jay Clayton, at 2 (Oct. 24, 2019), available at [https://www.cii.org/files/issues\\_and\\_advocacy/correspondence/2019/20191024%20SEC%20comment%20letter%20proxy%20advisor%20accuracy.pdf](https://www.cii.org/files/issues_and_advocacy/correspondence/2019/20191024%20SEC%20comment%20letter%20proxy%20advisor%20accuracy.pdf).





basis for its final rules, saying accuracy was never the “sole basis” for its proposal and falling back to a vague goal of wanting to “improve the overall mix of information available to investors.” In the words of an SEC Commissioner who dissented from the final rules, proxy advisor inaccuracy “failed as a justification for the proposal because there simply was not evidence of any significant error rate in proxy voting advice.”<sup>20</sup> In any event, we note that the SEC has reopened its 2020 rulemaking to address investor concerns with the rules that resulted from that proceeding. In short, there is no evidentiary basis for heightened monitoring responsibilities when an ERISA fiduciary uses the services of a proxy advisor.

This change will also avoid potential confusion. In its 2020 rulemaking, DOL never adequately explained when this provision applied or what it required. As DOL explains in its current proposal, since the general prudence and loyalty duties of ERISA already impose a monitoring requirement, the 2020 rule’s additional provision could have been misunderstood as requiring some special, undefined steps above and beyond these statutory obligations.<sup>21</sup>

### iii. Eliminating the Safe Harbors.

We also support DOL’s proposal to eliminate the two “safe harbor” examples in the 2020 rule –

- a. A policy of only voting on “particular types of proposals that . . . are substantially related to the issuer’s business activities or are expected to have a material effect on the value of the investment.” (DOL’s preamble had suggested such a policy might involve voting only on special situations, such as M&A transactions and contested elections of directors.); and
- b. A policy of not voting unless the plan’s holding of the company involved exceeds a threshold of the plan’s total holdings. (DOL’s preamble had suggested 5% as a possible threshold.).

As DOL notes, characterizing an aspect of the rule as a “safe harbor” invites it to be widely adopted, making it especially important that it adequately safeguard the interests of plan participants. DOL also notes the vagueness of the first safe harbor and that the second one has practical limitations, since

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<sup>20</sup> Statement of the Honorable Allison Herren Lee at SEC Open Meeting (July 22, 2020) (“Lee Open Meeting Statement”), available at <https://www.sec.gov/news/public-statement/lee-open-meeting-2020-07-22>; see also id. (“The final rules will still add significant complexity and cost into a system that just isn’t broken, as we still have not produced any objective evidence of a problem with proxy advisory firms’ voting recommendations. No lawsuits, no enforcement cases, no exam findings, and no objective evidence of material error—in nature or number. Nothing.”).

<sup>21</sup> We note some inconsistency in how this rule has been described in different places in the 2020 preambles, as well as in the preamble to the current proposal. See 86 Fed. Reg. at 57,281 (describing this rule as applying “where the authority to vote proxies or exercise shareholder rights has been delegated to an investment manager or where a proxy voting firm performs advisory services as to voting proxies”). By its terms, the current rule applies “[w]here the authority to vote proxies or exercise shareholder rights has been delegated to an investment manager pursuant to ERISA section 403(a)(2), or a proxy voting firm or other person who performs advisory services as to the voting of proxies.” We understand the rule, by its terms, to apply to situations where voting or other authority to exercise shareholder rights has been delegated to an investment manager or proxy advisor; indeed, that is the only reading of the rule that gives meaning to the word “who” in it. In addition, significant aspects of the rule would not make sense in the context of a proxy advisor that is only providing advice, but has no authority to make voting decisions. In any event, this ambiguity is an additional reason this part of the rule should be deleted or, if that is not pursued for some reason, clarified and re-proposed for comment.



many investment managers of sub-portfolios of ERISA investment vehicles would not necessarily have the information to calculate this threshold. At a more general level, DOL recognizes the two safe harbors, in conjunction with other provisions of the current rules, “may be construed as little more than regulatory permission for plans to broadly abstain from proxy voting.” At the same time, the new rule would retain language specifically allowing “fiduciaries [to] adopt proxy voting policies providing that the authority to vote a proxy shall be exercised pursuant to specific parameters prudently designed to serve the plan’s interest in providing benefits to participants and their beneficiaries and defraying reasonable expenses of administering the plan.”

Glass Lewis supports these changes. DOL never explained in the 2020 rulemaking how these safe harbors were consistent with a fiduciary’s general duties of prudence and loyalty to plan participants, let alone why ERISA should steer fiduciaries into them. The first safe harbor rests on an unexplained and unsupported premise that certain types of proxy votes -- in fact, the vast majority of proxy votes<sup>22</sup> -- are not “substantially related to the issuer’s business activities or are expected to have a material effect on the value of the investment.” As explained in Glass Lewis’ prior comment letter, however, shareholders’ voting rights, including the fundamental right to elect the company’s directors, largely derive from state corporate law.<sup>23</sup> In fact, as the Delaware Chancery Court has explained, the shareholder franchise “is critical to the theory that legitimates the exercise of power by some (directors and officers) over vast aggregations of property that they do not own.”<sup>24</sup> As a matter of federalism, statutory authority, and common sense, DOL should not try to substitute its own judgment about the proper scope of the shareholder franchise for that of the states and other corporate governance authorities.

Moreover, many of the topics that corporate law permits shareholders to have a say on -- for example, the election of directors or ratification of auditors -- play an important risk mitigation role. These types of issues are often prophylactic; they do not readily lend themselves to an analysis of whether they will lead to a material effect on the value of a plan investment.<sup>25</sup> As DOL itself has previously recognized, however, they are nonetheless critical to avoid risks to plans’ share capital over the long term.<sup>26</sup> Because this safe harbor encouraged fiduciaries to take a pass on these and most other proxy voting issues, it creates a genuine risk to plan participants’ long-term interests and should be dropped from the rule.

The second safe harbor is problematic for similar reasons. This safe harbor appears to be premised on the notion that not voting at most, or perhaps even all, meetings a plan would be entitled to vote at would be in plan participants’ best interests. DOL never explained or came close to substantiating this position, however. As noted in our previous comment letter, hypothetical (and counterfactual)

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<sup>22</sup> Elsewhere in its 2020 proposal, DOL acknowledged that the types of matters it saw as meeting this test -- M&A transactions, buy-backs, dilutive share issuances and contested elections of directors -- comprise 5.6% of all items state and other federal law entrusts to shareholder vote. DOL 2020 Proposing Release at 84.

<sup>23</sup> *Sante Fe Industries*, 430 U.S. at 479, 97 S.Ct. at 1304 (emphasis in original, quoting *Cort v. Ash*, 422 U.S. 66, 84, 95 S.Ct. 2080, 2090-91, 45 L.Ed.2d 26 (1975)).

<sup>24</sup> *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 659 (Del. Ch. 1988) (Allen, J.).

<sup>25</sup> The concept of “materiality” derives from the antifraud provisions of the federal securities laws. See *Basic, Inc. v. Levinson*, 485 U.S. 224, 240 (1988).

<sup>26</sup> See 2016 Interpretive Bulletin at 9.



“illustrations” in which proxy voting is costly and misleading discussion of the “mixed evidence” of the effectiveness of proxy voting are not a factual basis for such a rule.<sup>27</sup> There was simply no factual predicate established in the 2020 rulemaking to support seeking to steer ERISA fiduciaries into this practice. In addition, as DOL now notes, this safe harbor presents operational challenges that may make it practically unworkable.

Importantly, eliminating the safe harbors will not leave plan fiduciaries adrift with no guidance. As noted above, section (d)(3)(i) of the rule will continue to allow plan fiduciaries to “adopt proxy voting policies providing that the authority to vote a proxy shall be exercised pursuant to specific parameters prudently designed to serve the plan’s interest in providing benefits to participants and their beneficiaries and defraying reasonable expenses of administering the plan.” This sensible provision accords with current industry practice; many of our ERISA fiduciary clients, like our other clients, have adopted proxy voting policies to guide how they vote. Continuing to explicitly recognize the use of such policies in the rule gives fiduciaries the discretion they need to vote on behalf of their participants and beneficiaries in an effective and cost-efficient manner. Having such a policy, particularly one developed and implemented in an effective and cost-efficient manner with the assistance of an expert service provider, is evidence of a fiduciary’s prudence.<sup>28</sup>

#### iv. Eliminating Special Documentation Requirements.

Finally, DOL proposes to eliminate the requirement added in 2020 that plan fiduciaries “[m]aintain records on proxy voting activities and other exercises of shareholder rights.” DOL guidance has traditionally taken a more flexible, principles-based approach to documentation of fiduciary monitoring.<sup>29</sup>

Glass Lewis supports this change. As we noted in our 2020 comment letter, DOL never explained the need for adding new documentation requirements to the rule. In fact, DOL had previously explained that there is no basis to impose more onerous documentation requirements that would treat proxy voting differently than investment decisions or other activities of plan fiduciaries.<sup>30</sup> No evidence that DOL’s prior practical approach to documentation had created any problems or harmed plan participants in any way was adduced in the 2020 rulemaking. Absent such evidence, there is no need for a

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<sup>27</sup> See Glass Lewis Comment Letter at 5-10 and 24-26.

<sup>28</sup> See *Donovan v. Walton*, 609 F. Supp. 1221, at 1239-40 (S.D.Fla. 1985) (retaining and overseeing the work of expert consultants to help properly administer plan assets is evidence of a fiduciary’s prudent behavior).

<sup>29</sup> See, for example, Letter from Phyllis C. Borzi, Assistant Secretary for Employee Benefits Security, EBSA Response to Performance Audit Draft Audit Report Number 09-11-001-12-121 (Mar. 29, 2011) (“DOL 2011 OIG Response”) (“[A]s to fiduciary monitoring, various types of plan documentation of its ongoing operations may be sufficient to show appropriate monitoring of proxy voting decisions. Similarly, the rationale for a manager’s vote may be to follow a uniform internal policy for recurring issues, and simply to document the reasons for any vote which goes against the policy.”), available at <https://www.oig.dol.gov/public/reports/oa/2011/09-11-001-12-121.pdf>.

<sup>30</sup> DOL 2011 OIG Response (“In light of our enforcement and regulatory experience with proxy voting decisions, we do not believe we have a public record at this time that would justify the administrative burden and expenses that would be imposed on plans by a more expansive recordkeeping requirement than that described in the Interpretive Bulletin. Nor do we have a basis for uniquely singling out fiduciary proxy voting activities for a special documentation rule that does not apply to other fiduciary actions.”).



prescriptive rule on the subject and we support DOL's proposal to revert to its traditional, more flexible approach to documentation of fiduciary monitoring.

## Other Changes

In addition to the proposed changes, DOL should reconsider including sub-section (d)(2)(iii) in the final rule. This provision, which was newly added in 2020 and requires a specific determination when a fiduciary "adopt[s] a practice of following the recommendations of a proxy advisory firm or other service provider," is both unnecessary and unclear.

This provision was not proposed in its current form or as a standalone provision in 2020, meaning it has not benefited from the public comment process. While the provision is not well explained in the rushed and cursory preamble to the 2020 final rules, that preamble suggests that it responds to "the public comments that cited fiduciary practices that carry a high risk of noncompliance with ERISA." For the reasons discussed above and in our other comment letter, however, the record in that rulemaking, as well as the referenced SEC rulemaking, in no way, shape or form demonstrate that ERISA fiduciaries that seek the services of a proxy advisor are at "high risk of noncompliance with ERISA." To the contrary, by obtaining independent research and/or vote execution services, these fiduciaries will be more informed and better able to vote in an effective and cost-efficient manner.<sup>31</sup> For that reason, this provision is not only unnecessary, but potentially harmful to plan participants to the extent it suggests to ERISA fiduciaries that seeking expert advice and assistance with some aspects of proxy research and vote execution somehow risks noncompliance with ERISA.

It is also unclear what this provision means. As discussed above, the significant majority of our clients today receive recommendations based on their own custom voting policy or a "hybrid" policy that incorporates some elements of Glass Lewis "house policy," the client's custom policy, and/or issues that are "referred" for case-by-case analysis by the client. These clients have not "adopt[ed] a practice of following the recommendations of a proxy advisory firm" and we assume this part of the rule would not apply to them. Even for clients that elect to receive recommendations based on Glass Lewis house policy, however, those clients are in no way bound to follow those recommendations and they can and do depart from them based on their own determination of how to cast particular votes. While, in our experience, clients do not choose to receive recommendations based on a policy without first carefully reviewing it and deciding it reflects their chosen voting approach, that choice is not binding on them at any point. Unless DOL means for this part of the rule to only apply in the uncommon circumstance of a client that, for conflicts, regulatory prohibition, or some other reason, decides in advance that it will only vote in line with its proxy advisor or other service provider's recommendation, we are unclear when or how this provision would apply.

The Investment Duties regulation already provides -- in the immediately preceding sub-section -- that plan fiduciaries must exercise prudence and diligence in selecting and monitoring service providers, including proxy advisors. Because of this, including the additional vague and heightened burden of

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<sup>31</sup> See *Donovan*, 609 F. Supp. at 1239-40.



(d)(2)(iii) is both unnecessary and a potential deterrent to informed, responsible shareholder engagement.

## B. Investment Prudence and Loyalty Rules

Glass Lewis also supports the proposed changes to the investment prudence and loyalty duties section of the rule. Elements of the rules adopted in 2020 sought to discourage fiduciaries from considering environmental, social, and governance factors in their investment decisions. DOL had no legitimate basis to put such blinders on retirement plan fiduciaries and the resulting regulatory scheme exposes plan participants to some of the most significant risks to a long-term investor. The proposed changes are amply justified and should be adopted expeditiously.

The 2020 rulemaking was premised, in large part, on DOL's unsupported assumption that ERISA fiduciaries were considering ESG factors for "the purpose of achieving political or social objectives," rather than "maximizing return to beneficiaries." While this theory was pushed by self-interested corporate trade associations, it lacked any sound evidentiary basis and ignored the clear, emerging consensus view of some of the world's most sophisticated investors that ESG factors are important, material risk-return considerations. As State Street Global Advisors recently noted: "We believe that addressing material ESG issues is good business practice and essential to a company's long-term financial performance - **a matter of value, not values.**"<sup>32</sup> Commenting on the proposed rules in 2020, BlackRock told DOL: "We believe that sustainability-related factors can contribute to both value creation and value destruction.... [T]here is a robust body of research that reinforces these views."<sup>33</sup> And Fidelity Investments, in that same rulemaking, noted that DOL's skepticism of ESG "fails to appropriately acknowledge the extent to which plan fiduciaries increasingly utilize environmental, social or corporate governance considerations specifically as critical pecuniary factors in any investment strategy. ESG factors can incorporate long-term financial considerations that investors may not take into account when solely considering an investment's quantitative earnings model."<sup>34</sup>

In short, the 2020 rulemaking was premised on the advocacy positions of corporate trade associations and the preconception that fiduciaries are pursuing (disfavored) "political or social objectives" and must be stopped from doing so. Self-serving advocacy positions and unfounded assumptions are not a sound basis for rulemaking, however. ERISA's duty of prudence should reflect the best and most current

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<sup>32</sup> Letter from Cyrus Taraporevala, State Street Global Advisors, to Corporate Board Members (Jan. 28, 2020) (emphasis in original); see also Bank of America Merrill Lynch, "Equity Strategy Focus Point ESG Part II: a deeper dive," (June 15, 2017) (ESG investing would help investors avoid bankruptcies and ESG attributes "have been a better signal of future earnings volatility than any other measure [it has] found.").

<sup>33</sup> Letter of BlackRock to the Department of Labor at 1 (July 30, 2020), available at <https://www.blackrock.com/corporate/literature/publication/dol-financial-factors-in-selecting-plan-investments-073020.pdf>.

<sup>34</sup> Letter of Fidelity Investments to the Department of Labor at 5 (July 30, 2020) (emphasis removed), available at <https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB95/00673.pdf>.



thinking on investment and stewardship practices.<sup>35</sup> Investment theory and practice has evolved to recognize the materiality of many ESG considerations. These considerations should therefore be treated no differently than any other material economic consideration for ERISA purposes.

We support the specific changes DOL has put forward to correct course. In particular, we strongly support the proposal to eliminate the concept of only considering “pecuniary factors” and instead clarify that a prudent fiduciary may consider any factor material to the risk-return analysis, including climate change and other ESG factors. As DOL explains in the regulatory preamble, “material climate change and other ESG factors are no different than other ‘traditional’ material risk-return factors.”

While we recognize that the term “pecuniary” was drawn from ERISA case law, the term itself is antiquated, more used in legal than investment practice, and connotes something that can readily be monetized. For these reasons, the added need to determine that a consideration is a “pecuniary factor,” coupled with the 2020 preamble’s skepticism of ESG considerations, has created complexity and confusion, thereby potentially chilling ERISA fiduciaries from considering material risk-return factors. ESG factors -- such as the structure of a company’s board of directors, its human capital management practices, or how its business may be affected over the long term by climate change -- may be less readily susceptible to quantification in monetary terms than, for example, a balance sheet line item. That in no way means, however, that these factors may not be just as, if not more, critical to the long-term financial returns of the company’s investors, including retirement plan participants and beneficiaries. By eliminating the term “pecuniary” from the rule, DOL would free up fiduciaries to consider the full range of potential material risk-return factors without fear of regulatory second-guessing or litigation.

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<sup>35</sup> See Lukomnik Letter, quoting §227 of the Restatement (Third) of Trusts (“Trust investment law should reflect and accommodate current knowledge and concepts. It should also avoid repeating the mistake of freezing its rules against future learning and developments.”)



## Conclusion

For all the reasons stated above, Glass Lewis supports the proposed changes and encourages DOL to adopt them, as well as the other change discussed above. Thank you for your consideration of our comments.

Sincerely,

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October 5, 2020

Submitted online at [regulations.gov](https://www.regulations.gov)

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

Dear Acting Assistant Secretary Wilson:

Thank you for the opportunity to comment on “Fiduciary Duties Regarding Proxy Voting and Shareholder Rights,” the proposed rules recently issued by the Employee Benefits Security Administration of the Department of Labor (“DOL”).<sup>1</sup>

Glass, Lewis & Co., LLC (“Glass Lewis”) supports DOL’s stated objective of making sure that retirement plan fiduciaries are managing plan assets, such as voting and other shareholder rights, in the best interest of their plan participants. Glass Lewis’ primary business consists of providing research and advice to investors, including retirement plan fiduciaries, to enable them to effectively and efficiently make and execute proxy voting decisions in the best interest of their client

The proposed rules, however, seem intended to deter retirement plan fiduciaries from doing just that. Stemming from unsupported and incorrect assumptions that proxy voting and other shareholder engagement is ineffective and costly to plan participants, the proposed rules would create unworkable standards and mandate the use of unduly burdensome and risky analyses to justify voting proxies. The proposal would then except policies of not voting or

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<sup>1</sup> Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, RIN 1210-AB91, 85 Fed. Reg. 55,219 (Sept. 4, 2020) (the “Release”). Page references throughout are to the pdf version of the release made available by DOL.



voting with management from these burdens, incentivizing plans to either forgo exercising their shareholder rights or just adopt a policy of “robovoting” with management.

We are deeply concerned that the proposed rules would harm plan participants and the public interest. We are also concerned that DOL’s lack of prior consultation with market participants and rushed rulemaking process are not sufficient to adequately consider the issues involved and to fully understand the economic and practical consequences of its untested approach. For these and all the other reasons detailed below, we respectfully request that DOL not adopt the proposed rules and instead reaffirm the balanced approach in its current proxy voting guidance.

## **I. Background.**

### **A. Glass Lewis.**

Founded in 2003, Glass Lewis is a leading independent proxy advisor.<sup>2</sup> As a proxy advisor, Glass Lewis provides proxy research and vote management services to institutional investor clients throughout the world. While, for the most part, investor clients use Glass Lewis research to help them make proxy voting decisions, these institutions also use Glass Lewis research when engaging with companies before and after shareholder meetings. Further, through Glass Lewis’ Web-based vote management system, Viewpoint®, Glass Lewis provides investor clients with the means to receive, reconcile and vote ballots according to custom voting guidelines and record-keep, audit, report and disclose their proxy votes.

Glass Lewis serves more than 1,300 institutional investor clients — primarily public pension funds, mutual funds and other institutions that invest on behalf of individual investors and have a fiduciary duty to act, including through proxy voting, in the best interests of their beneficiaries. In 2019, Glass Lewis published over 26,000 proxy research reports on companies headquartered around the globe.

In addition to providing proxy research, Glass Lewis executes votes on behalf of its investor clients, in accordance with their specific instructions. A significant majority of Glass Lewis’ clients today have their own custom voting policies. During the policy formulation process, an institution will review Glass Lewis’ policies to assess the similarities and differences between the institution’s views and Glass Lewis’ “house policy.” Since Glass Lewis engages

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<sup>2</sup> Glass Lewis is a portfolio company of the Ontario Teachers’ Pension Plan Board (“OTPP”) and Alberta Investment Management Corp. (“AIMCo”). Neither OTPP nor AIMCo is involved in the day-to-day management of Glass Lewis’ business.



extensively with institutional investors and aims to have policies that reflect the views of its clients, it is not uncommon for an investor client to elect the same policy as Glass Lewis for some or all of the issues up for vote.

Once finalized, Glass Lewis helps these clients implement their policies by applying them to the circumstances presented by companies in their proxy statements and recommending how they vote accordingly. Glass Lewis does so through its vote management system, in which each ballot populates with recommendations based on the specific policies of the client, enabling the client to submit votes in a timely and efficient manner. (Under no circumstance is Glass Lewis authorized to deviate from a client’s instructions or to determine a vote that is not consistent with the policy specified by the client.) When a preliminary ballot is ready for review, the voting system will alert the client and provide such client with relevant disclosures and other information needed to review and evaluate the matters up for a vote. Clients can choose to restrict the submission of a ballot until after their authorized personnel have reviewed and approved the votes. Clients can also make — and often do make — changes to their preliminary ballots before signing off. And, assuming the voting deadline has not passed, they can even change their votes and resubmit them.

## **B. The role of proxy advisors.**

Glass Lewis believes that proxy advisors play an important support role, providing resources and technical, subject-matter expertise to help institutional investors meet their fiduciary responsibility to vote securities on behalf of their participants and beneficiaries in a cost-effective way. As the U.S. Securities and Exchange Commission (“SEC”) has explained, “When making voting determinations on behalf of clients, many investment advisers retain proxy advisory firms to perform a variety of functions and services . . . . Contracting with proxy advisory firms to provide these types of functions and services can reduce burdens for investment advisers (and potentially reduce costs for their clients) as compared to conducting them in-house.”<sup>3</sup>

As an increasing share of investors own stock indirectly, such as through mutual and pension funds, these individual investors are dependent on those institutional investors to vote on their behalf and act in their best interest. In order to do so both effectively and efficiently, those institutional investors often leverage their resources by using the services of a proxy advisor. As the Council of Institutional Investors and a coalition of investors have explained:

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<sup>3</sup> U.S. Securities and Exchange Commission, Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, Release No. IA-5325 at 5 (Aug. 21, 2019) (“SEC August 2019 Guidance”).



Retail holders now invest much of their capital with institutional investors because they understand that institutional investors' expertise and size bear the expectation of higher returns, lower costs and mitigated risks. Importantly, retail investors also understand that aggregating their individual holdings into larger, concentrated blocks through an institutional manager allows for more effective monitoring of company management.

Even so, institutional investors themselves face challenges in spending significant time and resources on voting decisions because the funds and other vehicles they manage receive only a portion of the benefits conveyed on all investors of the relevant enterprise.

Proxy advisors are a market-based solution to address many of these practical cost issues. Proxy advisors effectively serve as collective research providers for large numbers of institutional investors, providing these investors an affordable alternative to the high costs of individually performing the requisite analysis for literally hundreds of thousands of ballot proposals at thousands of shareholder meetings each proxy season.<sup>4</sup>

In addition, proxy advisors provide a viable solution for asset managers and other investors seeking a way to mitigate their own conflicts of interest when voting shares on behalf of their participants or beneficiaries. As the SEC has noted, an investment adviser "may look to the voting recommendations of a proxy advisory firm when the investment adviser has a conflict of interest, such as if, for example, the investment adviser's interests in an issuer or voting matter differ from those of some or all of its clients."<sup>5</sup> While the ultimate responsibility of voting proxies in the best interest of its clients continues to lie with the investment adviser, the SEC has signaled that "this third-party input into such an investment adviser's voting decision may mitigate the investment adviser's potential conflict of interest."<sup>6</sup>

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<sup>4</sup> Letter of Ken Bertsch, Executive Director, Council of Institutional Investors and 60 institutional investors to Chairman Jay Clayton, at 2 (Oct. 15, 2019), available at [https://www.cii.org/files/issues\\_and\\_advocacy/correspondence/2019/201910015proxy\\_advisor\\_sign\\_on\\_final.pdf](https://www.cii.org/files/issues_and_advocacy/correspondence/2019/201910015proxy_advisor_sign_on_final.pdf).

<sup>5</sup> SEC August 2019 Guidance at 5-6.

<sup>6</sup> Id.

## II. There is no need for the rules.

DOL has not shown any need for the proposed rules. None of the reasons DOL cites for its action provide any compelling reason to replace its current guidance or promulgate a new rule, and certainly not one with the effect of deterring plan fiduciaries from voting shares in the best interest of plan participants.

### A. Changes in the investment landscape make shareholder engagement more important, not less.

To demonstrate a need for these rules, DOL first points to “changes in the investment landscape” since the Avon Letter was issued in 1988. DOL notes that the share of individual company stock held in private pension funds has decreased, while an increasing percentage of plan investments are in mutual funds, many of which pursue passive investing strategies. DOL further notes the increasing role of institutional investors in the capital markets and that these shareholders’ proxy voting policies have become more complex over time.

What DOL does not explain is why these changes would warrant a new rule that seeks to discourage ERISA fiduciaries from exercising shareholder rights. If, as DOL’s current proxy voting guidance states and most fiduciaries believe, the costs of proxy voting are low and voting provides overall benefits to the plan, the portion of plan assets held in individual company stocks is irrelevant. In fact, if the percentage of plan assets in stocks is decreasing, that would suggest that proxy voting is less costly and less difficult for plans than in the past.<sup>7</sup> Further, DOL ignores the economies of scale that plans can achieve by delegating voting to asset managers, which, in turn, receive research and execution assistance from proxy advisors across their accounts. The growth of institutional investors and their increasingly sophisticated custom voting policies have made shareholder engagement all the more important and cost-effective. It is certainly not a reason to seek to prevent ERISA fiduciaries from engaging in it.

DOL also asserts that asset managers have mistakenly believed that shareholder voting and engagement contribute to shareholder value. According to DOL, however, emerging research “regarding whether proxy voting has reliable positive effects on shareholder value and a plan’s investment has yielded mixed results.”<sup>8</sup> And DOL takes particular issue with some investors’ focus on environmental, social and governance (“ESG”) risks, asserting that “[i]t is

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<sup>7</sup> DOL offers no evidence that plans’ positions in individual portfolio companies are smaller than in the past.

<sup>8</sup> Release at 13.

likely that many of these [recent environmental and social shareholder] proposals have little bearing on share value or other relation to plan interests.”<sup>9</sup>

But DOL offers scant evidence to second-guess market practices, experience, and the expert judgments of asset managers on this issue. DOL simply ignores strong evidence of the benefits of shareholder voting and engagement on companies’ financial performance, as well as the benefits, on an individual company and plan-wide basis, of considering systematic risks that fall under the ESG umbrella. In fact, DOL itself acknowledges the increasing sophistication and resources dedicated to shareholder voting and engagement, but offers no explanation for why this would be the case other than unsupported insinuations that plan fiduciaries must be pursuing their personal, political preferences or the illogical suggestion that asset managers spend significant resources to vote out of a mistaken belief it is required.

The simple reality is that fiduciaries have increasingly focused on proxy voting and shareholder engagement because it adds value, both for their individual investments and for the portfolio as a whole. Shareholder votes on the election of directors (which constitute a majority of proxy votes) convey important information about shareholders’ views and can and do affect companies’ decisions about who should serve as corporate directors.<sup>10</sup> A group of experienced practitioners and academics recently offered a concrete, monetized example of the financial benefits of engagement to a retirement plan’s beneficiaries:

As an example, consider the Boardroom Accountability Project undertaken by the New York City Comptroller, on behalf of the New York City retirement systems, in 2014. Comptroller Scott Stringer announced that he would seek to create a “proxy access” rule at 75 companies through private ordering . . . . The mere announcement caused a 53 basis point excess return, according to three academics, including one from the SEC. At the time of Comptroller Stringer’s announcement, the City’s funds held \$5.023 billion in those 75 companies’ stock. Based on the 53 basis points of excess return, that means

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<sup>9</sup> Release at 40.

<sup>10</sup> See for example Yaron Nili & Kobi Kastiel, *Competing for Votes*, 10 Harv. Bus. L. Rev. 287 (2020), available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3681541](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3681541) (“Shareholder voting matters. It can directly shape a corporation’s governance, operational and social policies. But voting by shareholders serves another important function—it produces a marketplace for votes where management and dissidents compete for the votes of the shareholder base. The competition over shareholder votes generates ex ante incentives for management to perform better, to disclose information to shareholders in advance, and to engage with large institutional investors.”).

the BAP created some \$266 million in excess return for the City's pension funds. As the City's funds generally hold 1% or less of a company's stock, that means the total market impact was more than \$25 billion. The actual impact on total market value over time, as 600 companies have adopted proxy access is likely even greater. While the academic study noted that the results likely would have been greater had a proxy access standard been market-wide and set by regulation, even just using the 53 basis point as the basis, extending the attempt to install proxy access across every listed company at the time of Stringer's announcement would have resulted in an increased market value of some \$132.5 billion.<sup>11</sup>

DOL also frames the issue narrowly - as whether "such activities [are] likely to enhance the value of a plan's investment *in a particular security*" - rather than focusing on the impact on the plan. But, as illustrated by this example, shareholder engagement at one company can have spillover effects on other plan holdings. Participants in a plan with a diversified portfolio of individual stocks would want to maximize the value of the portfolio as a whole, rather than each individual company, and a prudent fiduciary would therefore engage in activities that have a net positive effect for the plan as a whole.<sup>12</sup>

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<sup>11</sup> Letter from Jon Lukomnik, Keith Johnson et al. to the Department of Labor on the Proposed ESG Rule (July 21, 2020) ("Lukomnik Letter"), available at <https://corpgov.law.harvard.edu/2020/07/21/comment-letter-on-proposed-regulation-of-esg-standards-in-erisa-plans/>.

<sup>12</sup> This is why the quote from David Yermack that DOL uses to justify discouraging shareholder engagement actually demonstrates one of the reasons that DOL's approach is misguidedly narrow. See Ann Lipton, I Just Read the Department of Labor's New ERISA Voting Proposals and Boy Are My Fingers Tired (from typing) (Sept. 4, 2020) ("Lipton Blog"), [https://lawprofessors.typepad.com/business\\_law/2020/09/i-just-read-the-department-of-labors-new-erisa-voting-proposals-and-boy-are-my-fingers-tired-from-ty.html](https://lawprofessors.typepad.com/business_law/2020/09/i-just-read-the-department-of-labors-new-erisa-voting-proposals-and-boy-are-my-fingers-tired-from-ty.html). In fact, as Professor Lipton points out, DOL dropped the italicized part of Yermack's observation to obscure this very point: "Activist institutions frequently state that their goal is not to improve the value of individual investment positions, but rather to create positive externalities by signaling optimal governance practices market-wide, *potentially improving the value of the institutions' other diversified investments.*" (emphasis added).

DOL's other support for its claim of "mixed results" on the effectiveness of shareholder engagement, which are mostly studies of hedge fund activism, is also thin and selective. For example, the first article cited by DOL concluded that "shareholder activism has become more value increasing over time. Research based on shareholder activism from the 1980s and 1990s generally finds few consequential effects, while activism in more recent years is more



As to ESG considerations, DOL seeks to substitute its judgment for the emerging consensus view of some of the world’s most sophisticated investors. As State Street Global Advisors recently noted: “We believe that addressing material ESG issues is good business practice and essential to a company’s long-term financial performance - **a matter of value, not values.**”<sup>13</sup> BlackRock recently told DOL in a related rulemaking: “We believe that sustainability-related factors can contribute to both value creation and value destruction. . . . [T]here is a robust body of research that reinforces these views.”<sup>14</sup> And Fidelity Investments, in that same rulemaking, noted that DOL’s skepticism of ESG “fails to appropriately acknowledge the extent to which plan fiduciaries increasingly utilize environmental, social or corporate governance considerations specifically as critical pecuniary factors in any investment strategy. ESG factors can incorporate long-term financial considerations that investors may not take into account when solely considering an investment’s quantitative earnings model.”<sup>15</sup> ERISA’s duty of

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frequently associated with increased share values and operating performance.” Matthew R. Denes, Jonathan M. Karpoff & Victoria B. McWilliams, *Thirty Years of Shareholder Activism: A Survey of Empirical Research*, 44 J. Corp. Fin. 405, 407 (2017). Obviously, the current value of shareholder engagement - not what happened in the 1980s and 1990s - is what is relevant to this rulemaking. Likewise, the point of the Lund article is not that shareholder voting or engagement is not effective, but that, due to what the author believes is a free rider problem, “passive fund managers are not doing enough to push management to maximize shareholder welfare.” Dorothy S. Lund, *The Case Against Passive Shareholder Voting*, 43 J. Corp. Law 101, 104-105 (2018); see also *id.* at 113-14 (“In sum, although institutional investors’ incentives are imperfect, there is evidence that the presence of large, sophisticated investors with a financial interest in the long-term health of portfolio companies has become an important corporate governance safeguard.”).

<sup>13</sup> Letter from Cyrus Taraporevala, State Street Global Advisors, to Corporate Board Members (Jan. 28, 2020) (emphasis in original); see also Bank of America Merrill Lynch, “Equity Strategy Focus Point ESG Part II: a deeper dive,” (June 15, 2017) (ESG investing would help investors avoid bankruptcies and that ESG attributes “have been a better signal of future earnings volatility than any other measure [it has] found.”).

<sup>14</sup> Letter of BlackRock to the Department of Labor at 1 (July 30, 2020), available at <https://www.blackrock.com/corporate/literature/publication/dol-financial-factors-in-selecting-plan-investments-073020.pdf>.

<sup>15</sup> Letter of Fidelity Investments to the Department of Labor at 5 (July 30, 2020) (emphasis removed), available at <https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB95/00673.pdf>.

prudence should reflect the best and most current thinking on investment and stewardship practices, not the advocacy positions of corporate trade associations.<sup>16</sup>

Moreover, DOL ignores the important role of shareholder engagement in risk mitigation. DOL's own current proxy voting guidance notes that the "financial crisis of 2008 exposed some of the pitfalls of shareholder inattention to corporate governance and highlighted the merits of shareholders taking a more engaged role with the companies."<sup>17</sup> The release offers no reason to believe this is not still the case. Emerging academic research shows that shareholder attention to ESG issues can significantly reduce investment risk.<sup>18</sup> Professor John C. Coffee, Jr. has recently explained asset managers' need for ESG disclosure as part of their approach to investment risk mitigation:

Economic logic explains why diversified institutional investors want more ESG disclosures . . . . Put simply, the Capital Asset Pricing Model ("CAPM") posits that diversified investors are primarily interested in "systematic risk," because diversification protects (and even immunizes) them from unsystematic risk. Systematic risks are essentially risks that diversification does not protect against: for example, a national banking crisis, a pandemic, or sudden and irreversible climate change. [And] much ESG disclosure overlaps heavily with systematic risk."<sup>19</sup>

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<sup>16</sup> See Lukomnik Letter ("Trust investment law should reflect and accommodate current knowledge and concepts. It should also avoid repeating the mistake of freezing its rules against future learning and developments.") (quoting §227 of the Restatement (Third) of Trusts).

<sup>17</sup> Interpretive Bulletin 2016-01, 81 Fed. Reg. 95,879, at 9 (Dec. 29, 2016) ("2016 Interpretive Bulletin").

<sup>18</sup> Hoepner, Andreas G. F., Ioannis Oikonomou, Zacharias Sautner, Laura T. Starks and Xiaoyan Zhou, "ESG Shareholder Engagement and Downside Risk," AFA 2018 paper (Aug. 10, 2018), available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2874252](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2874252).

<sup>19</sup> John C. Coffee, Jr., ESG, Common Ownership, and Systematic Risk: How They Intersect (Sept. 14, 2020) (footnote omitted), available at <https://clsbluesky.law.columbia.edu/2020/09/14/esg-common-ownership-and-systematic-risk-how-they-intersect/>.

Notably, DOL apparently seeks to deter ERISA fiduciaries from voting on issues that are widely understood to be basic aspects of corporate transparency and accountability. In its *Citizens United* decision, the Supreme Court assumed shareholders could vote on such issues. *Citizens*

DOL also ignores fiduciaries' duty to consider the needs of all their plan participants, including those with investment time horizons significantly longer than management's expected tenure at the company. As a group of academics and investment professionals explained in response to DOL's proposed ESG investing rule:

[Y]ounger and older participants are likely to have differing investment risk tolerances, income generation needs and long-term capital growth expectations. By defaulting to a short-term bias, the proposal downplays materiality of ESG/sustainability risks and opportunities (e.g., those associated with climate change, misaligned executive compensation plans, workforce mismanagement, human rights violations, corporate culture, etc.) to which long horizon ERISA investors are exposed, even though they might not be evident in short-term financial metrics.<sup>20</sup>

In sum, DOL's skepticism about the benefits of shareholder voting and engagement is based on a thin and selective reading of a few studies and ignores market practices, experience, the views of the world's most sophisticated investors and other, more compelling academic research. However, even if DOL had established that the evidence on the effectiveness of shareholder engagement was "mixed," it would in no way be a rational basis for this rule proposal. Given that DOL itself has previously acknowledged the costs of proxy voting are low, there would need to be clear and compelling evidence of some harm from shareholder voting - rather than "mixed" evidence of its effectiveness - to rationally justify a rule that skews voting in this manner. Other than the completely speculative costs hypothesized in its illustration, however, DOL has identified no such harm.

#### **B. Fiduciaries do not vote out of a misunderstanding that it is always required.**

DOL also claims that there has been "a persistent misunderstanding among some stakeholders that ERISA fiduciaries are required to vote all proxies." Its support for this,

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*United v. FEC*, 540 U. S. 93 (2003) (relying in part on "the procedures of corporate democracy . . . With the advent of the Internet, prompt disclosure of expenditures can provide shareholders and citizens with the information needed to hold corporations and elected officials accountable for their positions and supporters. Shareholders can determine whether their corporation's political speech advances the corporation's interest in making profits . . .")

<sup>20</sup> Lukomnik Letter. This is one of the reasons that DOL's reliance on a few event studies of the filing of shareholder proposals is misguided. A prudent fiduciary would likely have a longer-term horizon than immediate stock price reaction.

however, mainly consists of a few assertions to that effect by management trade associations and corporate counsel. DOL itself has clearly told fiduciaries they do not need to vote all proxies in its prior guidance and DOL provides no evidence from its industry oversight that ERISA fiduciaries are, in fact, voting all proxies out of some mistaken belief. Our experience is that plans and their asset managers recognize they do not need to vote when the costs of doing so exceed the expected benefits, such as is the case in a variety of recurring circumstances involving both U.S. and foreign companies.

In fact, DOL's own statements contradict its contention here. DOL has previously noted that, based on its reviews of plans' proxy voting practices, "we believe the guidance EBSA has provided over the years has become well understood."<sup>21</sup> In this very release, DOL explains that asset managers see voting and shareholder engagement as a key part of a responsible, prudent investment strategy. Specifically, DOL cites approvingly a report that "investor voting behavior among owners of U.S. companies has changed significantly - perhaps almost revolutionarily - over the past two decades," and that, "for the overwhelming majority of share capital represented in the U.S., **voting is certainly no longer a compliance exercise.**"<sup>22</sup> DOL also attributes the rise in shareholder engagement to ERISA fiduciaries' "belief that participating in such activities was likely to enhance the value of a plan's investment in a particular security."<sup>23</sup> Likewise, in 2016, DOL expressed concern that its 2008 guidance "may have worked to discourage ERISA plan fiduciaries . . . from voting proxies and engaging in other prudent exercises of shareholder rights."<sup>24</sup> DOL makes no effort to reconcile any of these recent statements with its current contention that ERISA fiduciaries are voting all proxies based on a "persistent misunderstanding" of what it takes to comply with ERISA.<sup>25</sup>

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<sup>21</sup> Letter from Phyllis C. Borzi, Assistant Secretary for Employee Benefits Security, EBSA Response to Performance Audit Draft Audit Report Number 09-11-001-12-121 (Mar. 29, 2011) ("DOL 2011 OIG Response"), available at <https://www.oig.dol.gov/public/reports/oa/2011/09-11-001-12-121.pdf>.

<sup>22</sup> Release at 12 (emphasis added).

<sup>23</sup> Release at 13.

<sup>24</sup> 2016 Interpretive Bulletin at 4-5.

<sup>25</sup> The statement in a speech by a former, senior BlackRock official that under the Avon Letter, asset managers "should generally vote shares as part of their fiduciary duty" plainly does not reflect a misunderstanding that asset managers "must always vote proxies." In fact, it suggests a correct understanding of DOL's currently effective guidance. See 2016 Interpretive Bulletin at 5 (DOL guidance properly understood to mean that "proxies should be voted as part of the

### **C. Recent SEC actions are not a reason for DOL rulemaking.**

Finally, the DOL points to the SEC's recent issuance of guidance for investment advisers and adoption of rules governing proxy advisors. DOL acknowledges that "[m]any investment managers are registered as investment advisers with the SEC" and therefore are subject to the SEC guidance. DOL does not point to any significant regulatory gap left by the SEC's actions, however, nor does it explain why the SEC's adoption of one set of requirements related to proxy voting advice would necessitate DOL adopting a different set of requirements for ERISA fiduciaries. (We note that DOL has abandoned the claim in its rulemaking agenda that the goal of this rulemaking was to "harmonize" its requirements with those of the SEC.) In short, the SEC's actions do not provide any rational reason for DOL to impose further, different obligations on asset managers that are ERISA fiduciaries.

### **III. The proposed rules add onerous and unworkable burdens with no explanation or even acknowledgment of the change from its past guidance.**

The principal feature of the proposed rules is a new requirement that each decision to vote a proxy proposal be justified by what the DOL characterizes as "individual cost/benefit analyses."<sup>26</sup> Specifically, the new rules would add six factors that must be considered both in "deciding whether to exercise shareholder rights and when exercising shareholder rights." Among the mandatory considerations, the fiduciary must:

- Consider "only factors that they prudently determine will affect the economic value of the plan's investment;"
- "Investigate material facts that form the basis for any particular proxy vote;" and
- "Maintain records . . . that demonstrate the basis for particular proxy votes."

The requirement to consider these six factors would be reinforced by a new rule that a plan fiduciary "must not vote any proxy unless the fiduciary prudently determines that the matter being voted upon would have an economic impact on the plan after considering those factors described [above] and taking into account the costs involved (including the cost of research, if necessary, to determine how to vote)."

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process of managing the plan's investment in company stock unless a responsible plan fiduciary determined that the time and costs associated with voting proxies with respect to certain types of proposals or issuers may not be in the plan's best interest").

<sup>26</sup> Release at 27.

This is a significant change in the law. DOL’s current guidance on proxy voting was specifically issued to reassure fiduciaries that, absent unusual circumstances, they do not need to engage in a “cost-benefit analysis” before voting proxies. Now, however, the DOL would mandate that each proxy vote be justified through an individual cost-benefit analysis, including, among other things, a “determination” that the matter being voted on “would have an economic impact on the plan.” In fact, DOL’s proposal would make a series of changes that each would serve to make fiduciaries’ decision to exercise shareholder rights more difficult and costly. Among the changes (all emphasis added):

- The proposed rules would mandate that ERISA fiduciaries “must not vote any proxy unless the fiduciary prudently determines that the matter being voted upon *would have an economic impact* on the plan after considering those factors described [above] and taking into account the costs involved (including the cost of research, if necessary, to determine how to vote).”
  - DOL’s current guidance provides that “[t]he fiduciary obligations of prudence and loyalty to plan participants and beneficiaries require the responsible fiduciary to vote proxies on issues that *may affect the value* of the plan’s investment. *This principle applies broadly.*”
- The proposed rules would mandate that ERISA fiduciaries “[i]nvestigate material facts that form the basis for any particular proxy vote . . . .”
  - DOL’s current guidance does not use the word “investigate” or contain any equivalent requirement.
- The proposed rules would mandate that ERISA fiduciaries “consider[] *only* factors that they prudently *determine will affect the economic value* of the plan’s investment.”
  - DOL’s current guidance states that fiduciaries are required to “consider those factors that *may affect* the value of the plan’s investment.”
- The proposed rules suggest that only ballot items related to M&A, share issuances and contested elections of directors are “likely to have a significant impact on the value of the plan’s investment.”
  - DOL’s current guidance suggests that shareholder engagement would be appropriate in “various circumstances,” including --
    - “the independence and expertise of candidates for the corporation’s board of directors,”
    - “governance structures and practices,”
    - “executive compensation,”
    - “the nature of long-term business plans including plans on climate change preparedness and sustainability,”
    - “governance and compliance policies and practices for avoiding criminal liability and ensuring employees comply with applicable laws and regulations,”

- “the corporation's workforce practices (e.g., investment in training to develop its work force, diversity, equal employment opportunity),”
- “policies and practices to address environmental or social factors that have an impact on shareholder value,” and
- “other financial and non-financial measures of corporate performance.”
- The proposed rules would mandate that ERISA fiduciaries maintain “records on proxy voting activities . . . , including records that demonstrate *the basis for* particular proxy votes.”
  - DOL’s current guidance requires “records as to proxy voting.”
- The proposed rules say nothing about the importance of considering the potential value and cost-effectiveness of shareholder engagement in concert with other shareholders or the relevance of being a long-term, passive holder.
  - DOL’s current guidance specifically notes that shareholder engagement is consistent with ERISA when the fiduciary has “a *reasonable expectation* that such monitoring or communication with management, *by the plan alone or together with other shareholders*, is likely to enhance the value of the plan's investment in the corporation, after taking into account the costs involved,” and that “[s]uch a reasonable expectation may exist in various circumstances, for example, where plan *investments in corporate stock are held as long-term investments, where a plan may not be able to easily dispose of such an investment, or where the same shareholder engagement issue is likely to exist in the case of available alternative investments.*”

Each of these changes is significant on its own and would increase compliance costs and/or detract from ERISA fiduciaries’ ability to manage assets and mitigate risk in the best interest of plan participants. For example, the new standard of “determin[ing]” that a specific proxy vote “would have an economic impact” on the plan is completely ill-suited to the purpose and role of proxy voting. Many of the items corporate law permits shareholders to have a say on - for example, the election of directors or ratification of auditors - are to mitigate risk and assure prophylactic measures are in place to avoid threats to their share capital over the long term. Even if the company were to propose a director for election to the board who was clearly unqualified and incompetent, how would a fiduciary “determine” that voting against that person “would have an economic impact on the plan”? Requiring a definitive determination of economic impact for each proxy vote is unworkable and would effectively prevent fiduciaries from engaging in activities that would mitigate risk and enhance value for their plan participants.<sup>27</sup>

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<sup>27</sup> See also Brian Croce, DOL proposes rule to narrow scope of ERISA fiduciaries’ proxy voting, Pensions & Investments (Aug. 31, 2020), available at <https://www.pionline.com/regulation/dol-proposes-rule-narrow-scope-erisa-fiduciaries-proxy-voting> (quoting ERISA counsel: the



Other critical elements of the rules are equally problematic, as well as unexplained. No information is provided about what it means to “[i]nvestigate material facts that form the basis for any particular proxy vote,” although a fiduciary that votes without having done so would now risk violating ERISA. What is DOL’s basis for no longer considering issues long and widely understood to be financially material like “governance structures and practices” to be “likely to have a significant impact on the value of the plan’s investment”? Why would DOL no longer reference the relevance of being a long-term, passive holder?

While each of these unexplained changes is significant in its own right, in the aggregate, they amount to a complete shift from the generalized determination contemplated by the 2016 Interpretive Bulletin. Indeed, the sea change in approach is starkly reflected by the way DOL described the costs of the analysis it expected under its prior guidance versus the costs anticipated under the proposed rules. In 2016, DOL noted that:

**In most cases, proxy voting and other shareholder engagement does not involve a significant expenditure of funds by individual plan investors** because the activities are engaged in by institutional investment managers . . . . Those investment managers often engage consultants, including proxy advisory firms, in an attempt to further reduce the costs of researching proxy matters and exercising shareholder rights . . . . **Thus, . . . many proxy votes involve very little, if any, additional expense to the individual plan shareholders to arrive at a prudent result.**<sup>28</sup>

Now, however, DOL estimates that researching and documenting these analyses would take asset managers from 40 minutes (for routine items) to 2 hours and 20 minutes (for special situations) for each proxy vote, resulting in an aggregate compliance burden to ERISA plan asset managers of well over \$10 billion dollars a year.

Notwithstanding that this is the central feature of the proposal, the release devotes all of two sentences to summarizing the 2016 Interpretive Bulletin and does not discuss or even mention the significant differences detailed above. DOL does, however, propose rescinding that Interpretive Bulletin, which, of course, would be unnecessary if DOL were not changing its requirements through the proposed rules.<sup>29</sup>

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proposed rule “could present real practical challenges in that benefits from shareholder engagement are often long term in nature. So we’ll have to look at the rule carefully in order to see if this is remotely workable in the real world.”).

<sup>28</sup> 2016 Interpretive Bulletin at 5-6 (emphases added; footnote omitted).

<sup>29</sup> See Lipton Blog.

“[A]n agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored. Failing to supply such analysis renders the agency's action arbitrary and capricious.”<sup>30</sup> As the Supreme Court explained in a recent case, an agency “must at least display awareness that it is changing position and show that there are good reasons for the new policy.”<sup>31</sup>

DOL has not met that basic standard here. Each of the changes should be explained and justified with “good reasons for the new policy.” DOL - perhaps recognizing that there are no such good reasons<sup>32</sup> - has completely failed to do so and elected to ignore the fact that it is changing the law. This fails to meet its standards under the APA and the proposal should be withdrawn or reissued for comment with some reasoned explanation for the changes.

#### **IV. The documentation requirements are unnecessary and unworkable.**

The proposal’s documentation requirements are both unnecessary and unnecessarily specific. First, DOL would impose a new requirement for fiduciaries to maintain records “that demonstrate the basis for particular proxy votes.” Then, DOL would add an additional requirement that, in monitoring an asset manager or proxy advisor, the fiduciary “require such investment manager or proxy advisory firm to document the rationale for proxy voting decisions or recommendations sufficient to demonstrate that the decision or recommendation was based on the expected economic benefit to the plan, and that the decision or recommendation was based solely on the interests of participants and beneficiaries in obtaining financial benefits under the plan.”

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<sup>30</sup> *Lone Mtn. Processing, Inc. v. Sec’y of Labor*, 709 F.3d 1161, 1164 (D.C. Cir. 2013) (internal quotations and citations omitted).

<sup>31</sup> *Encino Motorcars, LLC v. Navarro*, 136 S.Ct. 2117, 2126 (2016) (internal quotations omitted). Moreover, the agency must “be cognizant that longstanding policies may have engendered serious reliance interests that must be taken into account.” *Id.* (internal quotations and citations omitted).

<sup>32</sup> DOL later acknowledges these analyses would be so burdensome that engaging in them would be “a likely inefficient use of plan resources.” Release at 27.

But DOL does not explain the need for either of these new requirements. In fact, DOL has previously explained that there is no basis to impose more onerous documentation requirements that would treat proxy voting differently than other fiduciary activities:

[A]s to fiduciary monitoring, various types of plan documentation of its ongoing operations may be sufficient to show appropriate monitoring of proxy voting decisions. Similarly, the rationale for a manager's vote may be to follow a uniform internal policy for recurring issues, and simply to document the reasons for any vote which goes against the policy.<sup>33</sup>

DOL does not provide evidence that the practical documentation requirements in its current guidance have created any problems or harmed plan participants' interest in any way.

Likewise, the proposed documentation requirement for each decision or recommendation by an asset manager or proxy advisor is also problematic. While it is unclear exactly what DOL expects here, if the suggestion is that proxy advisors would tailor their rationale for every recommendation to each specific plan (and its participants) whose asset manager uses its research, that would be unnecessarily plan-specific and unworkable given the scale of proxy advisors' work. As described above, proxy advisors support their clients, such as asset managers for retirement plans, by providing vote recommendations based on their chosen proxy voting policy, which is usually a custom policy the client has selected to serve the interests of its clients (e.g., a retirement plan and its participants). The proxy advisor does not, in any way, make the determination of what a client's policy should be and how a client should vote. These decisions are at the sole discretion of the asset manager.

This new documentation requirement is also unnecessary. Under the proposed rules, an ERISA fiduciary may only follow the recommendations of a proxy advisor if, among other things, it has determined that the proxy advisor's guidelines "are consistent with the economic interests of the plan and its participants and beneficiaries." In addition to making this determination, the rules would require ERISA fiduciaries to supervise their proxy advisor on an ongoing basis.<sup>34</sup> Adding to these requirements a mandate that each rationale somehow make a

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<sup>33</sup> DOL 2011 OIG Response; see also *id.* ("In light of our enforcement and regulatory experience with proxy voting decisions, we do not believe we have a public record at this time that would justify the administrative burden and expenses that would be imposed on plans by a more expansive recordkeeping requirement than that described in the Interpretive Bulletin. Nor do we have a basis for uniquely singling out fiduciary proxy voting activities for a special documentation rule that does not apply to other fiduciary actions.").

<sup>34</sup> Proposed Rule 29 C.F.R. 2550.404a-1(e)(2)(ii)(D) and Release 22 n.56.

plan-specific demonstration would achieve little other than adding potentially significant additional cost.

**V. Designating voting with management or not voting as “permitted practices” is arbitrary and capricious.**

Having saddled ERISA fiduciaries with these arbitrarily burdensome analyses, the proposal would then offer them a way to avoid them – the “permitted practices” of voting with management or not voting. The proposal makes clear that DOL believes its proposal would effectively compel use of the permitted practices: DOL “anticipates that most, if not all plans, will adopt policies that utilize the permitted practices.”<sup>35</sup> And, in fact, this is the purported benefit of the proposal: “The Department anticipates that plans would derive savings from the proposal’s ‘permitted practices,’” by which it apparently means they would not then incur the unreasonable costs of the arbitrarily burdensome analyses its rules would otherwise mandate.<sup>36</sup> DOL, however, does not explain how these permitted practices are even consistent with a fiduciary’s general duties of prudence and loyalty under ERISA Section 404, let alone provide a rational basis for steering fiduciaries into these practices.

Shareholders’ voting rights are granted by state corporate law and, to a lesser extent, exchange listing standards (and, in the case of say-on-pay, federal legislation). As the Delaware Supreme Court has explained:

The most fundamental principles of corporate governance are a function of the allocation of power within a corporation between its stockholders and its board of directors. The stockholders' power is the right to vote on specific matters, in particular, in an election of directors . . . Accordingly, while these "fundamental tenets of Delaware corporate law provide for a separation of control and ownership," the stockholder franchise has been characterized as the "ideological underpinning" upon which the legitimacy of the directors managerial power rests.<sup>37</sup>

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<sup>35</sup> Release at 51; see also *id.* at 59 (“The Department intends that the permitted practices will impact a large share of all proxy votes . . .”).

<sup>36</sup> Release at 50; see also *id.* at 59 (“the burden associated with these votes when using the permitted practices will likely be very low”).

<sup>37</sup> *MM Cos., Inc. v. Liquid Audio, Inc.*, 813 A.2d 1118, 1126 (Del. 2003) (citations omitted); see also *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 659 (Del. Ch. 1988) (shareholder vote “is

State corporate law therefore grants shareholders the right to vote on certain matters that are essential to safeguarding the capital they have provided the corporation, such as the election of directors, ratification of auditors, and changes to the articles of incorporation or bylaws. State corporate law, as well as exchange listing standards, also mandate that shareholder approval be obtained before management engages in self-interested transactions, such as the adoption of a stock option plan for the company’s officers and directors.

Through its permitted practices, however, DOL seeks to second-guess the expert judgments of these recognized corporate governance authorities. Thus, DOL’s second permitted practice encourages fiduciaries to only vote on matters “substantially related to the corporation’s business activities or likely to have a significant impact on the value of the plan’s investment,” which DOL suggests are M&A transactions, buy-backs, dilutive share issuances and contested elections of directors. As DOL elsewhere notes, these types of votes comprise 5.6% of all items entrusted to shareholder vote by state and federal law.<sup>38</sup> While votes on these matters are certainly important, the DOL does not explain its conclusion that the other 94% of situations in which shareholders have a right to vote are routine and somehow not “substantially related to the corporation’s business activities” or otherwise are inappropriate issues for shareholders to weigh in on.

For example, under the Dodd-Frank Act, shareholders of public companies are entitled to an advisory vote on the company’s executive compensation program. By doing so, shareholders can evaluate executive compensation relative to company performance and express their disapproval for pay without performance. The DOL proposal, however, would inexplicably treat these votes as not “substantially related to the corporation’s business activities or likely to have a significant impact on the value of the plan’s investment.”<sup>39</sup> In contrast, however, the proposal would permit an ERISA fiduciary to depart from its usual practice of not voting if the company’s management needed them to vote to achieve quorum for a shareholders’ meeting. According to the proposal, “The direct and indirect costs incurred by the corporation related to delaying the shareholders’ meeting, such as additional proxy

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critical to the theory that legitimates the exercise of power by some (directors and officers) over vast aggregations of property that they do not own.”).

<sup>38</sup> Release at 84.

<sup>39</sup> This directly contradicts prior DOL positions. See, for example, DOL 2011 OIG response (“plan fiduciaries should independently evaluate proposals regarding executive compensation and “golden parachute” arrangements because of the reasonable expectation that such proposals will economically impact the value of the company.”)



solicitation, legal, and administrative costs, **would be an economic detriment to the plan’s holding.**<sup>40</sup> DOL should explain why plan participants would be harmed by the administrative costs of delaying an annual meeting, but not by excessive pay without performance.

As to voting with management, DOL’s primary argument is that ERISA fiduciaries can rely on the recommendations of officers and directors because they have fiduciary duties to the company under state corporate law. But the law imposes these duties because management’s interests can and do differ from those of the company’s shareholders,<sup>41</sup> and state corporate law requires shareholder votes precisely because managers’ fiduciary duties alone are not adequate to align management’s and shareholders’ interests.

In fact, courts often lightly enforce these duties on the basis that shareholders have other means to oversee management, such as proxy voting. For example, in *In re Walt Disney Co. Derivative Litigation*,<sup>42</sup> the Delaware Chancery court held that a company’s board of directors did not breach its fiduciary duty by allowing the company to pay an executive who was quickly hired and fired \$140 million for 14 months’ work. The court explained that “Delaware law does not - indeed, the common law cannot - hold fiduciaries liable for a failure to comply with the aspirational ideal of best practices,” and that “[t]he redress for failures that arise from faithful management must come from the markets, **through the action of shareholders** and the free flow of capital, and not from this Court.”<sup>43</sup>

Moreover, fiduciary duties do not mandate good business performance. As the Delaware courts have explained, “Generally, shareholders have only two protections against perceived inadequate business performance. They may sell their stock . . . or **they may vote to**

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<sup>40</sup> Release at 28 n.63 (emphasis added).

<sup>41</sup> Adolf A. Berle, Jr. & Gardiner C. Means, *The Modern Corporation and Private Property* (1932) (“The separation of ownership from control produces a condition where the interests of owner and of ultimate manager may, and often do, diverge, and where many of the checks which formerly operated to limit the use of power disappear.”)

<sup>42</sup> 907 A.2d 693 (2005).

<sup>43</sup> *Id.* at 698 (emphasis added); see also Lipton Blog (shareholder “rights [to sue for breach of a fiduciary duty] are *extremely limited* because *state corporate law relies on the shareholder franchise*; it’s why the courts can take a hands-off approach to management matters, because they assume *shareholders* will do the monitoring, not the judiciary.)

**replace incumbent board members.**<sup>44</sup> And, as DOL itself recognizes in its current guidance, “selling the stock and finding a replacement investment may not be a prudent solution for a plan fiduciary.”<sup>45</sup> In fact, that guidance quotes Vanguard founder John Bogle’s explanation that index funds’ “only weapon” if management is not performing is to “get a new management or to force the management to reform.”<sup>46</sup> Making it difficult for fiduciaries to use the shareholder franchise to incentivize good business performance would affirmatively harm plan participants’ interests.

The DOL also defends robovoting with management because “nearly all management proposals are approved with little opposition.”<sup>47</sup> But this is akin to arguing that a bank doesn’t need a security guard because most days no one tries to rob it. The value of the shareholder franchise comes from the ability to exercise it when needed (even if in a small percentage of cases) and management’s knowledge that any of their proposals could be met with similar disapproval. After all, management may no longer feel constrained to offer proposals that are usually acceptable to their shareholders if federal regulations prevent shareholders from voting on them.

The DOL offers no rational explanation of why routinely voting for the proposals of someone with divergent interests than plan participants, including on matters like executive pay,<sup>48</sup> would be consistent with a fiduciary’s duties of loyalty and prudence, let alone why ERISA should favor it.

The arbitrariness of designating voting with management or not voting (unless management needs it to achieve a quorum) as permitted practices is exacerbated by DOL’s

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<sup>44</sup> *Blasius*, 564 A.2d at 659 (emphasis added).

<sup>45</sup> 2016 Interpretive Bulletin at 6.

<sup>46</sup> *Id.* at 6-7.

<sup>47</sup> Release at 26.

<sup>48</sup> George W. Dent, *Toward Unifying Ownership and Control in the Public Corporation*, 1989 Wis. L. Rev. 881, 891 (“Managerial and shareholder interests also diverge over executive compensation. Managers want high pay for little work; shareholders favor the opposite.”), available at [https://scholarlycommons.law.case.edu/cgi/viewcontent.cgi?article=1513&context=faculty\\_publications](https://scholarlycommons.law.case.edu/cgi/viewcontent.cgi?article=1513&context=faculty_publications).





decision to encourage these practices, rather than the market practices that have developed for institutional shareholders to effectively and efficiently safeguard their clients' interests through proxy voting. As the 2016 Interpretive Bulletin recognized:

The maintenance by an employee benefit plan of a statement of investment policy designed to further the purposes of the plan and its funding policy is consistent with the fiduciary obligations set forth in ERISA section 404(a)(1)(A) and (B). Since the fiduciary act of managing plan assets that are shares of corporate stock includes the voting of proxies appurtenant to those shares of stock, a statement of proxy voting policy would be an important part of any comprehensive statement of investment policy.<sup>49</sup>

As noted above, the super-majority of Glass Lewis' clients have developed their own custom voting policy to ensure votes are cast consistently and in their clients' best interests. Moreover, DOL's current guidance recognizes that investment managers may, after appropriate due diligence, select and use a proxy advisor both to achieve cost-savings and to help implement its chosen voting policy in an informed and consistent manner. The proposal, however, would arbitrarily make voting in line with management recommendations a permitted practice, rather than an asset managers' use of a customized proxy voting policy developed to serve its clients' best interests. DOL should preserve the recognition in its 2016 guidance that an expert, appropriately-designed "statement of investment policy designed to further the purposes of the plan" is consistent with ERISA's fiduciary duties.

Indeed, the release is laced throughout with the unsupported allegations of proxy advisor critics, without DOL either substantiating those criticisms or noting their makers' self-interest.<sup>50</sup> For example, the release refers to issuer trade associations' claims that proxy advisors have made what the release calls "factual and/or analytic errors." But this issue was thoroughly explored as part of the recent SEC proxy advisor rulemaking. There, as here, issuers and their advocacy groups expressed "concerns" about errors in proxy advice and the SEC proposed an issuer prereview regime to "promote accuracy" in proxy advice.<sup>51</sup> The comment

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<sup>49</sup> 2016 Interpretive Bulletin at 14.

<sup>50</sup> See Release at 42, 43, 44 (alleged problems of proxy advisors are prefaced with "some commenters have asserted," "A number of stakeholders have questioned," "Some question," "the SEC described concerns," "Some stakeholders also question," and "Critics additionally complain").

<sup>51</sup> U.S. Securities and Exchange Commission, Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice, Release No. 34-87457 (Nov. 5, 2019).

process in that rulemaking, however, revealed that these “concerns” were anecdotes and generalized allegations based on surveys; there simply was no evidence of a significant error rate in proxy advice. The SEC’s own Investor Advisor Committee demonstrated that a chart used by the SEC in its proposal reflected that issuers only claimed proxy advice errors 0.3% of the time and “none of those [were] shown to be material or to have affected the outcome of the related vote.”<sup>52</sup> Even with respect to this small number of claimed errors, an analysis by the Council of Institutional Investors revealed that “most of the claimed “errors” actually [were] disagreements on analysis and methodologies, and that some other alleged proxy advisory firm errors derive from errors in the company proxy statements.”<sup>53</sup> Tellingly, the SEC disavowed its claim of proxy advisor inaccuracy as the basis for its final rules, saying accuracy was never the “sole basis” for its proposal and falling back to a vague goal of wanting to “improve the overall mix of information available to investors.” In the words of an SEC Commissioner (who dissented from the final rules), proxy advisor inaccuracy “failed as a justification for the proposal because there simply was not evidence of any significant error rate in proxy voting advice.”<sup>54</sup>

Here, though, DOL would resuscitate this disproved “concern,” along with other unsubstantiated allegations, as part of the basis for its proposal. DOL should rely on evidence, not unsubstantiated concerns or the claims of self-interested parties. More generally, the proposal is arbitrary in expressing concern about asset manager and proxy advisor conflicts, while encouraging ERISA fiduciaries to rely on management recommendations or simply

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<sup>52</sup> See Recommendation of the SEC Investor Advisory Committee Relating to SEC Guidance and Rule Proposals on Proxy Advisors and Shareholder Proposals at 5 (Jan. 24, 2020) (emphasis in original), available at <https://www.sec.gov/comments/s7-22-19/s72219-6698769-206000.pdf>.

<sup>53</sup> Letter of Ken Bertsch, Executive Director, Council of Institutional Investors to SEC Chairman Jay Clayton, at 2 (Oct. 24, 2019), available at [https://www.cii.org/files/issues\\_and\\_advocacy/correspondence/2019/20191024%20SEC%20comment%20letter%20proxy%20advisor%20accuracy.pdf](https://www.cii.org/files/issues_and_advocacy/correspondence/2019/20191024%20SEC%20comment%20letter%20proxy%20advisor%20accuracy.pdf).

<sup>54</sup> Statement of the Honorable Allison Herren Lee at SEC Open Meeting (July 22, 2020), available at <https://www.sec.gov/news/public-statement/lee-open-meeting-2020-07-22>; see also id. (“The final rules will still add significant complexity and cost into a system that just isn’t broken, as we still have not produced any objective evidence of a problem with proxy advisory firms’ voting recommendations. No lawsuits, no enforcement cases, no exam findings, and no objective evidence of material error—in nature or number. Nothing.”).

automatically vote with management without addressing or even acknowledging management's conflicting interests.<sup>55</sup>

Finally, the DOL should clarify the operation of the permitted practices. In the proposal, the DOL claims that adopting the permitted practices will save plans' money by eliminating the need to analyze each proposal. However, the DOL also claims that the permitted practices will allow for individualized exceptions, such as where there is a "heightened management conflict[] of interest" or the company needs the plan to vote to achieve quorum for its annual meeting. These two goals are inconsistent. If an ERISA fiduciary avoids the costs of analyzing each proposal, they would have no apparent way of knowing if the proposal presents a heightened management conflict or otherwise poses special risks to the plan.<sup>56</sup>

## **VI. The economic analysis is flawed.**

DOL's regulatory impact analysis consists of qualitative discussion of the expected costs and benefits of the rules, as well as an "illustration" that quantifies the proposed rules' costs and benefits. The impact analysis and accompanying illustration have at least four fundamental flaws.

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<sup>55</sup> For example, the release notes that some proxy advisors "may issue proxy voting recommendations while the company that is the subject of such recommendations is a client of the firm's consulting business," and warns ERISA fiduciaries that "[p]articular attention" must be paid to such firms. Release at 22. It is not rational, however, to simultaneously warn ERISA fiduciaries about the proxy advice of someone who has consulted for a company, while encouraging them to unquestioningly accept the proxy advice of someone actually employed by the company (i.e., management). Compare also Release at 20-21 ("Information that will better enable fiduciaries to determine whether or how to vote proxies on particular matters includes . . . voting recommendations of management") with Release at 22 ("fiduciaries must be aware that conflicts of interest can arise at proxy advisory firms that could affect vote recommendations").

<sup>56</sup> As discussed further below, DOL's assumed cost savings also ignore the realities that most asset managers for ERISA plans will continue to vote proxies, and assume the related costs, for their non-ERISA clients. Moreover, even consistently voting with management would require the overhead costs of having a proxy voting platform and related systems and processes. Finally, DOL does not suggest that adopting a permitted practice will relieve ERISA fiduciaries from their broader obligation to monitor the corporate governance of portfolio companies.

First, DOL presents no actual evidence of a problem warranting this new regulation. While DOL expresses concern about the costs of proxy voting on plan participants, it provides no evidence of plan assets being wasted or spent imprudently on proxy voting. In fact, DOL is forced to admit that, based on the evidence it has, plans' costs for proxy voting "might generally seem small."<sup>57</sup> Assuming high costs as part of a hypothetical illustration is not evidence of a problem warranting regulatory intervention.

Second, and critically, the release fails to understand the baseline against which the proposed changes should be measured. Benefits and costs must be measured against a "baseline" and that "baseline should be the best assessment of the way the world would look absent the proposed action."<sup>58</sup> Here, however, DOL's assumed "baseline" has no grounding in current law or evidence of actual market practice. As noted above, DOL's current guidance makes clear that individual cost-benefit analyses are not required and that "many proxy votes involve very little, if any, additional expense to the individual plan shareholders to arrive at a prudent result." DOL nonetheless blithely asserts that "the activities described in the proposal already are reflected in common practice and are best practices."<sup>59</sup> No basis is given for this assertion,<sup>60</sup> however, and DOL admits it "lack[s] data" on the issue. In reality, it defies all logic to assume that asset managers as a "best practice[]" are spending what, by DOL's calculation, comes to some \$13 billion annually on compliance measures that DOL has specifically told them that they do not need to do.<sup>61</sup> Essentially, DOL has assumed away any obligation to justify the

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<sup>57</sup> Release at 40. DOL follows this admission with speculation that plans' actual costs might be higher and then weakly offers that "even small costs may not be justified."

<sup>58</sup> OMB Circular A-4, Regulatory Analysis (Sept. 17, 2003).

<sup>59</sup> Release at 51; see also Release at 58 ("the Department believes that the common practices of most plans related to proxy voting are generally consistent with the standards in the proposal").

<sup>60</sup> The only reference to actual facts about market practices is an admission that those facts do not support the assumed baseline. See Release at 52 (as to documentation, "such practices are not universal. In the course of its enforcement activity, the Department sometimes encounters instances where documentation is absent or does not meet the requirements of this proposal.")

<sup>61</sup> Table 2 indicates that a 5% increase in research costs and 1% increase in documentation costs would together would result in \$535,217,964 in additional, annual compliance costs for ERISA asset managers. Extrapolating from these figures, DOL's estimate of the total, annual compliance cost for ERISA asset managers to vote proxies is \$13,008,824,800.



costs of the burdensome analyses its rules would impose by assuming, with no basis, those analyses are being conducted today. This is an improper end-run around a cost-benefit analysis.<sup>62</sup>

Third, DOL's economic analysis and the accompanying illustration, in particular, ignore the role of proxy advisors in achieving economies of scale. The front part of the release acknowledges the "resource-intensive" tasks that an ERISA plan or its asset manager would need to take on to vote proxies, including "organizing proxy materials, diligently analyzing portfolio companies and the matters to be voted on, determining how the votes should be cast, and submitting proxy votes to be counted."<sup>63</sup> And it also notes that the cost "to collect and analyze the information necessary to reach an appropriate conclusion" "may be lower if the fiduciary can rely on an impartial, expert third-party adviser who specializes in such matters and provides similar services to many shareholders."<sup>64</sup> In fact, the economies of scale achieved through the use of asset managers and proxy advisors are part of the reason "voting proxies involves *very little, if any, additional expense* to the individual plan shareholders to arrive at a prudent result," as DOL's current guidance notes.

These facts are ignored in the illustration, however. The illustration assumes that some 2,000 asset managers will individually and independently perform a cost-benefit analysis, research and document their rationale for each proxy vote, without using a proxy advisor. As other parts of the release seem to recognize, however, this would not make economic sense and is not, in fact, how the proxy voting market works. The illustration thus assumes unrealistic costs that would be "saved" through use of the permitted practices. If DOL is going to rely on a theoretical illustration, that exercise should be reperformed with a more accurate model of how proxy voting works and then re-exposed for comment.

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<sup>62</sup> DOL's related assumptions that research costs will increase by 5% and documentation costs by 1% to account for asset managers who are not already complying with the proposed rule is equally unsupported, illogical and self-serving. Absent evidence, which we do not believe exists, that asset managers are already conducting individual cost-benefit analyses and complying with the other elements of the rule, DOL's economic analysis should acknowledge and quantify the full costs of all affected ERISA fiduciaries' complying with the new requirements.

<sup>63</sup> Release at 24.

<sup>64</sup> Release at 37; see also *id.* at 42 (noting SEC statement that "proxy advisory firms can capture economies of scale for several of the services they provide, including voting advice.")

Fourth and finally, the proposed rules' approach of focusing on economic impact to each individual portfolio company imposes the opportunity cost of causing ERISA fiduciaries to disregard systematic risks that cut across their portfolio. As discussed above, a variety of issues the rules would deter voting on, such as board declassification, may have positive, spillover effects beyond the company that is the subject of the engagement. The prescriptive requirement in the proposed rules that plan fiduciaries "must . . . consider[] only factors that they prudently determine will affect the economic value *of the plan's investment*" would effectively put blinders on fiduciaries, causing them to have to disregard these broader effects and their benefits to the plan as a whole.<sup>65</sup> This opportunity cost is not mentioned in the release's economic analysis, let alone considered and quantified. Regulations, especially "economically significant" ones, are supposed to be based on evidence and have their costs and benefits quantified to the extent possible.<sup>66</sup> DOL has not met that standard here.

## **VII. Legal issues.**

### **A. The rules exceed DOL's authority under ERISA by passing over into corporate governance.**

By displacing state corporate law with its own judgment about the proper scope of the shareholder franchise and by creating vastly differential compliance burdens based on how a shareholder votes, DOL has exceeded its authority to implement the general duties of prudence and loyalty under ERISA Section 404. "Corporations are creatures of state law, and investors commit their funds to corporate directors on the understanding that, except where federal law *expressly* requires certain responsibilities of directors with respect to stockholders, state law will govern the internal affairs of the corporation."<sup>67</sup>

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<sup>65</sup> In fact, in some circumstances, the excessively narrow approach mandated by the proposed rules would lead to the irrational result of ERISA plans actually voting against themselves. See Lipton Blog (citing Leo E. Strine, Jr., *Securing Our Nation's Economic Future: A Sensible, Nonpartisan Agenda to Increase Long-Term Investment and Job Creation in the United States*, 71 Bus. L. 1081, 1093 (2016)).

<sup>66</sup> Executive Order No. 13,563, 76 FR 3821, (Jan. 21, 2011) ("each agency is directed to use the best available techniques to quantify anticipated present and future benefits and costs as accurately as possible.")

<sup>67</sup> *Santa Fe Industries v. Green*, 430 U.S. 462, 479 (1977) (emphasis in original) (quoting *Cort v. Ash*, 422 U.S. 66, 84 (1975)).

Here, however, the permitted practices would substitute DOL’s opinion of what is “substantially related to the corporation’s business activities or likely to have a significant impact on the value of the plan’s investment” for the determinations made under state corporate law of what shareholders must approve or vote on. But the general provisions of ERISA Section 404 do not grant DOL authority to rewrite state corporate law; in fact, they should be read in a manner not to do so.<sup>68</sup>

Likewise, states’ decisions in their corporate law to grant shareholders a say on certain corporate matters can obviously be subverted if DOL can attach any degree of onerous conditions and liability risk to how shareholders vote on those matters (i.e., against management). Could DOL pass a rule saying all ERISA fiduciaries must vote against board declassification proposals because, in DOL’s opinion, those are bad corporate governance and would harm plans’ interests? Could DOL put in place an interim final rule during a contested merger saying only a vote for the merger would be a permitted practice, with massive compliance burdens and unworkable determinations required to justify an against vote?<sup>69</sup> The proposed rules would set a precedent for federal regulation that dictates the vote in internal corporate decisions governed by state corporate law. This is bad policy and beyond DOL’s general authority to make sure retirement plan fiduciaries are prudent and loyal.

For this reason also, we question the assertion in DOL’s “Federalism Statement” that the proposed rules would not have any direct effect on “the distribution of power and responsibilities among various levels of government.” The proposed rule taxes shareholders’ exercise of their rights under state corporate law based on their choice to exercise that right or to vote a particular way. “Delaware courts have long exercised a most sensitive and protective regard for the free and effective exercise of voting rights.”<sup>70</sup> Here, however, DOL would

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<sup>68</sup> *Bond v. United States*, 572 U.S. 844 (2014) (statute “must be read consistent with principles of federalism inherent in our constitutional structure”); *Business Roundtable v SEC*, 905 F.2d 406, 412 (D.C. Cir. 1990) (state corporate law “regulates the distribution of powers among the various players in the process of corporate governance, and the Commission’s present leap beyond disclosure is just that sort of regulation”); cf. *Am. Equity v. SEC*, 613 F.3d 166, 178 (D.C. Cir. 2010) (invalidating SEC rule for failure to adequately consider rule’s interaction with state law).

<sup>69</sup> Cf. *Business Roundtable*, 905 F.2d at 411 n.6 (“ If this part of the rule could allow the Commission to pass on the merits of a corporate merger, then the Commission was asserting a quite radical power.”).

<sup>70</sup> *Blasius*, 564 A.2d at 659 n.2.



intentionally deter exercise of those rights. DOL should explain how this is consistent with a due regard for the principles of Federalism.

### **B. The proposed rules would violate the First Amendment**

ERISA fiduciaries engage in speech and expression protected by the First Amendment when they vote and conduct other shareholder engagement activities that the proposed rules would apply to, such as “campaigning for shareholder proposals.”<sup>71</sup> The proposed rules are unquestionably a content-based and viewpoint-based restriction on such speech. They impose unique and burdensome restrictions on shareholder activities that may be contrary to the interests of a favored group, while removing those restrictions when the expressive activity favors the preferred group. Such laws “are presumptively unconstitutional and may be justified only if the government proves that they are narrowly tailored to serve compelling state interests.”<sup>72</sup> Here, that showing has not and cannot be made. In fact, far from demonstrating that the proposed rules are narrowly tailored to address a compelling state interest, the vague and unsupported speculation about plan assets being wasted on proxy voting underlying this proposal suggest the real motivation is to alter votes and suppress other expressive activity with which DOL does not agree.<sup>73</sup>

### **C. A 30-day effective period is not legal or appropriate.**

DOL states that its proposed rule would be effective 30 days after the date of publication of the final rule.<sup>74</sup> The release, however, acknowledges that OMB has designated the proposed rule as a “major rule,”<sup>75</sup> and the Congressional Review Act provides that a major

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<sup>71</sup> Release at 41.

<sup>72</sup> *NIFLA v. Becerra*, 538 U.S. \_\_\_ (2018) (quoting *Reed*, 135 S. Ct. at 2226).

<sup>73</sup> *First Nat'l Bank of Boston v. Bellotti*, 435 U.S. 765 (1978) (claim of waste not sufficient to prevent company from exercising its First Amendment rights); see also Victor Brudney, *Business Corporations and Stockholders' Rights Under the First Amendment*, 91 *Yale L.J.* 235, 251 (1981) (“when the stricture seems to be aimed at only a very narrow kind of political speech, and only on a particular topic, a court may reasonably suspect that the concern of the legislature is not “waste” but silencing the expression of particular views”).

<sup>74</sup> Proposed Rule 29 C.F.R. 2550.404a-1(g); Release at 32.

<sup>75</sup> Release at 35.

rule shall not be effective earlier than 60 days after publication of the final rule in the Federal Register.<sup>76</sup>

Moreover, given settled reliance interests and the importance of not disrupting the complex shareholder voting process, DOL should allow a significantly longer effective period for any final rule it adopts that, like the proposal, would force substantial changes to ERISA fiduciaries' voting practices. For example, the SEC recently included transition periods of well over a year for elements of its proxy advisor rules and shareholder proposal rules that would require market participants to adopt new policies and procedures and that would undo settled reliance interests. If DOL proceeds with a final rule, it should include an effective date that is consistent with the law and that is appropriate in the circumstances.

**D. A 30-day comment period with no access to other comments is inappropriate.**

DOL should also extend the comment period for at least two reasons. First, a 30-day comment period is too short for a rulemaking that: 1) would constitute the first rules under ERISA on proxy voting; 2) per DOL's own analysis, either imposes hundreds of millions in costs or results in hundreds of millions in savings based on how market participants respond to the rules; 3) OMB has designated a "major rule" under the Congressional Review Act; and 4) OMB has designated "economically significant." Especially considering the lack of data in the proposal, a 30-day comment period is too short for commenters to have a meaningful opportunity to react to what has been proposed and supply the agency with the information it should have to make informed decisions on this critical issue.<sup>77</sup>

Here, the harms of this short comment period have been exacerbated by DOL's failure to make comments it has received available to the public through its online portal. As of October 5, 2020, the last day of the comment period, none of the 208 comment letters that DOL has received have been made available on regulations.gov. This prevents commenters from being able to respond to other comments and deprives the agency of this critical input.<sup>78</sup>

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<sup>76</sup> 5 U.S.C. 801(a)(3)(A). DOL's own decision about when to conduct this rulemaking is not "good cause" for an exception to these requirements.

<sup>77</sup> Executive Order No. 12,866, 58 FR 51735, (Oct. 4, 1993) ("In addition, each agency should afford the public a meaningful opportunity to comment on any proposed regulation, which in most cases should include a comment period of not less than 60 days.")

<sup>78</sup> See Administrative Conference of the United States, Recommendation 2011-2 (June 16, 2011); see also Office of Information & Regulatory Affairs, Memorandum for the President's Management Council on Increasing Openness in the Rulemaking Process—Improving Electronic



DOL should extend or reopen the comment period to allow adequate time for comment and to permit commenters to respond to other comments.

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## Conclusion

For all the reasons stated above, Glass Lewis respectfully requests that the DOL not adopt the proposed rules and, instead, reaffirm the balanced approach in its current proxy voting guidance that affords plan participants the benefits of shareholder voting and engagement at low cost. Thank you for your consideration of our comments.

Sincerely,

Kevin Cameron  
Executive Chair

Nichol Garzon-Mitchell  
Senior Vice President, General Counsel

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Dockets at 2 (May 28, 2010) (“OMB expects agencies to post public comments and public submissions to the electronic docket on Regulations.gov in a timely manner, regardless of whether they were received via postal mail, email, facsimile, or web form documents submitted directly via Regulations.gov.”); cf. *Portland Cement v. Ruckelshaus*, 486 F.2d 375, 393 (D.C. Cir. 1973) (“It is not consonant with the purpose of a rule-making proceeding to promulgate rules on the basis of inadequate data, or on data that, [to a] critical degree, is known only to the agency.”).