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October 2, 2020

Submitted Electronically  
Office of Regulations and Interpretations  
Employee Benefits Security Administration  
U.S. Department of Labor

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

Dear Sir or Madam:

I am writing on behalf of Capital Group to comment on the Department of Labor's proposal to amend the fiduciary responsibility rules of ERISA to impose new requirements on the exercise of proxy voting rights. Capital Group is one of the oldest and largest asset managers in the nation. Through our investment subsidiaries, we actively manage approximately \$2 trillion in assets in separate accounts and various collective investment vehicles. Most of the assets we manage are in the American Funds family of mutual funds.

As discussed more fully below, we believe that without material changes the proposal will impose significant costs on plans and commingled funds, create undue risks for investment managers and other fiduciaries and ultimately harm plan investors. We strongly urge the Department to provide plan fiduciaries with greater flexibility to decide when to vote proxies by eliminating the bright-line distinction in the proposal between matters upon which proxy voting is required and prohibited. While we agree that there are matters where it is appropriate for a plan fiduciary to forego voting, the proposed rule is far too prescriptive as drafted and fails to allow investment managers and other fiduciaries the flexibility to pursue investor value broadly.

Under the proposal, plan fiduciaries and investment managers who have been delegated authority to vote proxies under ERISA section 405(c)(1) would have an obligation to vote proxies "where the fiduciary prudently determines that the matter being voted upon would have an economic impact on the plan" after taking into account only factors that "will affect the economic value of the plan's investment"

and the cost involved in voting; it would prohibit voting in all other circumstances. It would also stipulate that investment managers with proxy voting responsibility must “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.”

The preamble to the proposal explains that the Department’s proposed approach of effectively shifting the default from voting to not voting absent a determination of economic materiality is based on a handful of concerns, including managers’ potentially subordinating the interests of participants to unrelated objectives by voting on socially-directed proxy initiatives, a persistent misunderstanding by plan fiduciaries that voting is always required, and the Department’s perception that shareholder voting has not lived up to its promise of enhancing shareholder value relative to its costs.

At Capital Group, we believe in the value of proxy voting and consider it to be an integral part of our investment process. We do not delegate proxy voting responsibility to, or defer to the recommendations of, proxy advisory firms. Proxy proposals are evaluated in-house, with a dedicated team of 17 associates<sup>1</sup> who support our investment professionals in the evaluation of proxy proposals and the development of voting recommendations for proxies across all of our mandates, including collective investment trusts, separate accounts and mutual funds.

We appreciate that there are some matters for which it is appropriate for an investment manager to forego voting. In our experience, however, these matters are the exception, not the rule. Some proxy matters directly affect the economic value of a security, for example, a shareholder vote on a merger. For other shareholder votes, it may be prudent to vote even though it may not be clear that a matter “will affect” the value of a security. There is not, for example, a linear relationship between the value of a security and the composition of the issuer’s board of directors. However, there is an abundance of evidence that diverse decision-making bodies make better decisions. As a result, a board with a wide variety of perspectives makes it more likely that the company will make sound decisions that will enhance the value of the company’s stock.

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<sup>1</sup> As of June 30, 2020.

Moreover, we question whether it makes sense to focus on economic materiality solely with respect to the issuer at hand. There are many situations in which a proxy vote is material as it affects an industry or corporate governance in general but not as it impacts the value of a particular issuer. For example, shareholder votes on executive compensation may not be likely to directly affect the value of a plan's assets but there is little question that discouraging excessive compensation is in the long-term economic interests of the plan. More generally, the very presence of proxy voting encourages companies to engage in best practices. A vote, for example, on the selection of an independent auditor may not directly affect the value of a security but the vote reinforces the importance of an independent audit and draws attention to independent audits as a best practice.

An exclusive focus on the economic impact of a vote also misses an important aspect of proxy voting, namely the role it plays in allowing investment managers and other fiduciaries to accurately value companies. A vote on disclosure of corporate information, for example, reporting on hazardous materials included in products sold, may not make the company more valuable but it allows an investment manager to more accurately value the company, which directly affects investment decisions. And, more generally, proxy votes provide investment managers with insights into management's thinking and business approach which contribute to better valuations.

Put simply, we value proxy voting for reasons that are fundamentally economic in nature, but we take a broad, long-term view of what may affect the value of a plan's holdings. While certain proxy proposals may not appear at the outset to have a measurable economic impact on ERISA plan assets, we believe that over time the cumulative effect of having less shareholder engagement with, and accountability of, companies will undermine plan investment returns.

Moreover, investment managers like Capital Group leverage their scale to deliver proxy voting at little, if any, cost to clients. We do not charge transactional fees for proxy voting. There is no cost to our investors for any proxy vote. The costs we incur for proxy voting are paid from the management fees we receive. These costs are material when viewed in isolation but de minimus when considered across our investor base. We have scale and decades of experience with proxy voting. As a result, the implied cost for any given investor is so modest that we do not discount our management fee if a plan chooses to retain proxy voting responsibility while delegating other investment management responsibilities to us.

We do not foresee any cost savings to ERISA plans from the proposal, which would effectively default plans to not voting proxies except where there is a definable economic impact to the vote. We vote proxies on portfolio securities across all of our mandates, including mutual funds, collective investment trusts, separate accounts and non-US investment vehicles. This approach means that we are engaged in proxy voting regardless of any special rules under ERISA. As a result, the most likely outcome of the Department's proposal would be that investment managers will suppress most proxy voting for ERISA plan-asset mandates, notwithstanding that the managers are doing all of the work and research to vote proxies and there is no incremental cost associated with voting proxies for ERISA plans.

Contrary to its stated objective of reducing proxy voting-related costs incurred by plan fiduciaries, we believe the proposed rule will substantially increase plan costs by obligating investment managers to determine whether a proxy vote is economically material and document that determination. The addition of an economic materiality determination will add cost to the process. We appreciate the notion in the proposal of "permitted practices" to ease the burden of sorting through every vote but these practices would generate little savings. The first two practices – (1) voting with management except where matters are likely to have a significant impact on the value of the plan's investment and (2) voting only on matters that the fiduciary has previously determined will have a significant economic impact – do little to simplify the screening process. These practices define what action an investment manager should take once it has determined that a proxy matter is not economically material but still require the manager to determine whether a matter will have an economic impact – either concurrently or in advance of a vote. The third practice – refraining from voting unless the plan's holding is significant, such as 10 percent or more of the plan's assets – makes little sense for an investment manager who may be holding billions of dollars of a given security across the mandates it manages, even though any given plan's holdings are less than, for example, 10 percent of the plan's assets. The fact that a vote may have only a modest impact on a given plan should not mean that the fiduciary must ignore the cumulative impact across multiple investment vehicles.

This requirement is also problematic because the determination of whether a proxy vote is economically material is inherently qualitative and fundamentally a prediction about an uncertain future. Even qualified investment professionals will frequently have different views about materiality. It makes more sense to simply vote if the

matter at hand may affect the economic value of the plan's assets, at least where the cost of voting is insignificant.

We also fear that economic materiality determinations, particularly in conjunction with the documentation requirement noted below, will lead to costly and unpredictable class action litigation. There will inevitably be second guessing about economic materiality and we can anticipate lawsuits alleging that a vote was improper and seeking disgorgement of management fees.

Finally, the requirement for investment managers and other investment fiduciaries to document economic materiality will deplete resources as managers work to explain the rationale for each decision to vote or not vote a proxy. This will be particularly challenging for plan fiduciaries who must oversee investment managers, for example, in the common circumstance in which a plan has more than one investment manager and these managers are taking inconsistent positions on the economic materiality of the same proxy votes.

For these reasons, we urge the Department to reconsider the binary "must or must not" vote requirement. We believe instead that the proposal should reflect fundamental principles of fiduciary responsibility, including the duty of care and loyalty. In our view, these principles (i) prohibit voting on matters that would subordinate the interests of the plan to unrelated social goals; (ii) require voting where the proposal will affect the economic value of the security (taking into account costs); and (iii) permit voting in all other situations, including where the vote may affect the value of the security or the plan's assets as a whole (taking into account costs) or may help the fiduciary value the company.

This formulation has several virtues. First, it would prohibit voting where there is no possible economic nexus to the plan, i.e., where voting would subordinate the interests of the plan to unrelated objectives. This would help ensure that shareholder votes are not used to accomplish non-pecuniary goals. Second, it would clarify that voting is not required unless the fiduciary determines that there will be an economic impact from the matter at hand on the value of the security. This would be particularly helpful to smaller plans that may not have the resources necessary to effectively research proxy votes and may have to incur costs to acquire the necessary expertise. At the same time, it would allow investment managers who have scale and experience to vote proxies in the ordinary course where the cost of voting is de minimus and the manager determines that the proxy will not subordinate the interests of participants and beneficiaries to unrelated social goals. Third, it would reduce

unnecessary litigation and eliminate the burdensome materiality determination where the cost of voting is de minimus and preserve flexibility for investment managers to pursue value. In this regard, we believe that it will be relatively easy to determine whether a vote is on an entirely non-pecuniary matter. The vast majority of matters that are put to a shareholder vote have an obvious nexus to the issuer's business. Fourth, it would be an approach that is more closely harmonized with the Investment Advisers Act of 1940 (the "Advisers Act"), which like ERISA provides for a principles-based approach to proxy voting grounded in the fiduciary duties of care and loyalty. The Advisers Act does not prescribe a particular default for proxy voting but, instead, requires the investment adviser to make any voting determination in the best interest of the client and to not place the investment adviser's own interests ahead of the interests of the client.

In short, we believe the approach we recommend will address the concerns the Department has identified while preserving flexibility for investment fiduciaries to pursue economic value broadly.

We appreciate your consideration and would be happy to answer any questions. Please call the undersigned if we can be helpful at 213-615-4007.

Sincerely,



Jason K. Bortz  
Senior Counsel