

October 5, 2020

Via Electronic Filing

Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210
Attention: Proxy Voting and Shareholder Rights NPRM

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

Ladies and Gentlemen:

The Investment Adviser Association (**IAA**)¹ appreciates the opportunity to comment on the Department's proposed amendments to the "Investment duties" regulation under Title I of the Employee Retirement Income Security Act of 1974, as amended (**ERISA**).² The Proposed Amendments address proxy voting and related policies and the selection and monitoring of proxy advisory firms.

We respectfully urge the Department to withdraw this rulemaking, which represents a significant departure from how plan fiduciaries currently view their proxy voting responsibilities. The Proposed Amendments would substantially increase costs for plans and fiduciaries without providing measurable benefits to participants and beneficiaries. The Department has not demonstrated economic harm to plans, participants, and beneficiaries from current proxy voting practices that would justify these costs or that would support the Department's rationale for the Proposed Amendments, namely that proxy voting may not be in the economic interests of plan participants and beneficiaries.

¹ The IAA is the largest organization dedicated to advancing the interests of investment advisers registered with the Securities and Exchange Commission (**SEC**). For more than 80 years, the IAA has been advocating for advisers before Congress and U.S. and global regulators, promoting best practices and providing education and resources to empower advisers to effectively serve their clients, the capital markets, and the U.S. economy. The IAA's member firms manage more than \$25 trillion in assets for a wide variety of individual and institutional clients, including pension plans, trusts, mutual funds, private funds, endowments, foundations, and corporations. For more information, please visit www.investmentadviser.org.

² *Fiduciary Duties Regarding Proxy Voting and Shareholder Rights*, 85 FR 55219 (Sept. 4, 2020), available at <https://www.govinfo.gov/content/pkg/FR-2020-09-04/pdf/2020-19472.pdf> (**Proposed Amendments**).

We do not object to the Department making clear that a fiduciary is not required to vote all proxies, and that a fiduciary should have a written proxy voting policy that is reasonably designed to ensure that it votes in the best interest of the plan, its participants, and beneficiaries.³ However, the Proposed Amendments go well beyond this approach.

Regarding proxy advisory firms, we believe that the Department should recognize the wide variety of services provided by such firms and not take steps that reduce fiduciaries' access to essential services provided by these firms. We recommend that the Department align its approach with that taken by the SEC regarding the use of proxy advisory firms by SEC-registered investment advisers,⁴ or wait to take action regarding the use of proxy advisory firms until the SEC's recent actions in this area have been implemented.⁵

The Department Has Not Provided Sufficient Justification for the Proposed Amendments

The Department has proposed these regulations “due to significant changes in the way ERISA plans invest and in the investment world more broadly since the Department first spoke formally on these topics, a persistent misunderstanding among some stakeholders that ERISA fiduciaries are required to vote all proxies, and in light of recent actions by the [SEC] related to the proxy voting process.”⁶ The Department also expresses concern that “some fiduciaries and proxy advisory firms—in part relying on the Avon Letter—may be acting in ways that unwittingly allow plan assets to be used to support or pursue proxy proposals for environmental, social, or public policy agendas that have no connection to increasing the value of investments used for the payment of benefits or plan administrative expenses, and in fact may have

³ As the Department notes in the preamble to the Proposed Amendments (**Preamble**), SEC-registered investment advisers are subject to Rule 206(4)-6 under the Investment Advisers Act of 1940 (**Advisers Act**), which requires advisers to have written policies and procedures that are reasonably designed to ensure that advisers vote proxies in the best interest of their clients. Among other things, the procedures must include how an investment adviser addresses material conflicts that may arise between the adviser's interests and the interests of its clients. The Department also notes the SEC's guidance to investment advisers regarding proxy voting in 2019 and 2020. *See Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers*, Rel. No. IA-5325 (Aug. 21, 2019), available at <https://www.sec.gov/rules/interp/2019/ia-5325.pdf> (**SEC 2019 Guidance**); and *Supplement to Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers*, Rel. No. IA-5547 (July 22, 2020), available at <https://www.sec.gov/rules/policy/2020/ia-5547.pdf> (**SEC 2020 Guidance**).

⁴ *See* SEC 2019 Guidance and SEC 2020 Guidance.

⁵ *See* Exemptions from the Proxy Rules for Proxy Advice, Rel. No. 34-89372 (July 22, 2020), available at <https://www.sec.gov/rules/final/2020/34-89372.pdf>.

⁶ 85 FR at 55220.

unnecessarily increased plan expenses.”⁷ We believe that the Department has not shown that a problem exists with respect to how ERISA fiduciaries meet their fiduciary duty in connection with their voting of proxies, and the Proposed Amendments are therefore not warranted. We also do not believe that the Proposed Amendments address the Department’s concerns.

The Department’s proposed rule amendments would *prohibit* a plan fiduciary from voting any proxy unless the fiduciary “prudently determines that the matter being voted upon would have an economic impact on the plan.”⁸ A plan fiduciary would be *required* to vote on any matter that it prudently determines would have an economic impact on the plan.⁹ As discussed more fully below, the idea that a fiduciary would be able to determine conclusively whether each proxy vote, by itself, would have an economic impact is not realistic, including because it does not take into account a fiduciary’s long-term approach to its investment strategy or that a fiduciary may not have a view into all of a plan’s holdings. The Proposed Amendments also do not address the Department’s stated concerns about the costs of proxy voting. Both shareholders and issuers benefit from a cost-effective proxy voting process. However, the costs associated with attempting to comply with the Proposed Amendments would far exceed the current costs associated with proxy voting.

The Department describes as a benefit of the Proposed Amendments “societal resources freed for other uses due to voting fewer proxies.”¹⁰ We are troubled by the Department’s view that ERISA plans voting fewer proxies is a benefit. It does not take into account that voting rights that attach to securities owned by a plan may be considered an asset of the plan, and the ability to vote proxies is an intrinsic benefit of share ownership that allows shareholders to have a say in the governance of the companies they own. We also question the Department’s assessment that voting fewer proxies saves “societal resources.” We believe that this is a short-term view that does not factor in the long-term horizons of retirement investors and their fiduciaries. We simply do not agree that less proxy voting by ERISA plans is beneficial in and of itself.

⁷ 85 FR at 55222 (footnote omitted). In the Avon Letter, the Department stated that, “In general, the fiduciary act of managing plan assets which are shares of corporate stock would include the voting of proxies appurtenant to those shares of stock.” Letter to Helmut Fandl, Chairman of the Retirement Board, Avon Products, Inc. (Feb. 23, 1988). For the IAA’s comments on the Department’s proposal regarding ESG investing, *see* Letter from Gail C. Bernstein, IAA General Counsel, *Financial Factors in Selecting Plan Investments* (RIN 1210-AB95) (July 30, 2020), available at https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/about/Comment_Letter_Compilations/2020/IAA_Comment_Letter_-_ESG_Proposal.pdf.

⁸ Proposed Rule 404a-1(e)(3)(ii).

⁹ Proposed Rule 404a-1(e)(3)(i).

¹⁰ 85 FR at 55231.

The Proposed Binary “Economic Impact” Decision is an Unworkable and Costly Framework to Evaluate Proxy Voting

The Department has taken the view in the Proposed Amendments that, for each and every proxy vote, there either is or is not a net economic impact and that this impact is clearly discernable at the time of deciding whether to vote. In the Preamble, the Department states that “[i]nformation that will better enable fiduciaries to determine whether or how to vote proxies on particular matters includes the cost of voting, including opportunity costs; the type of proposal (e.g., those relating to social or public policy agendas versus those dealing with issues that have a direct economic impact on the investment); voting recommendations of management; and an analysis of the particular shareholder proponents.”¹¹ The Department goes on to state that “fiduciaries must be prepared to articulate the anticipated economic benefit of proxy-vote decisions in the event they decide to vote.”¹² The Proposed Amendments provide that fiduciaries would be required to consider the likely impact of the proxy vote on investment performance based on factors such as “the size of the plan’s holdings in the issuer relative to the total investment assets of the plan, the plan’s percentage ownership of the issuer, and the costs involved.”¹³

Even when taking all of these factors into account, the Preamble does not explain how a fiduciary would make the economic impact decision for every proxy, and how the fiduciary’s decision-making process would be evaluated in connection with that consideration. For example, a fiduciary may not be able to evaluate these factors with certainty because a plan may hold the same security through multiple fiduciary investment managers, and each manager may not be aware of positions held through other managers. Moreover, if a fiduciary received a proxy for a slate of directors recommended by a company’s management, for example, how would the fiduciary calculate “the opportunity costs” associated with the vote for each candidate? Also, how would the fiduciary “articulate the anticipated economic benefit” with respect to each candidate? There are more questions than answers associated with this “economic benefit” approach.

We believe that this binary approach as to whether a particular proxy vote does or does not have a net economic impact is not a workable framework to evaluate proxy voting. Instead, we believe that the appropriate framework is whether a fiduciary uses a prudent process for proxy voting, including a written proxy voting policy that is reasonably designed to ensure that the securities are voted in the best interest of the plan, participants, and beneficiaries. This approach is consistent with that taken by the SEC in the Advisers Act proxy voting rule (Rule 206(4)-6).

¹¹ 85 FR at 55224 (footnote omitted).

¹² *Id.*

¹³ Proposed Rule 404a-1(e)(2)(ii)(B).

We also do not believe that plan fiduciaries that are SEC-registered investment advisers should be required to have a proxy voting policy for their ERISA clients that differs from that for their non-ERISA clients where the policy is reasonably designed to operate in the best interest of both sets of clients. In the Regulatory Impact Analysis, the Department requests comment on whether asset managers use “uniform proxy policies” for both ERISA plans and other investors, and raises concern that uniform voting “may sometimes jeopardize responsible fiduciaries’ satisfaction of their duties under ERISA.”¹⁴ However, the Department goes on to say that:

[T]his concern may be mitigated in the case of investment managers subject to the SEC’s jurisdiction by the fact that federal securities law requires investment advisers to make the determination in their client’s best interest and not to place the investment adviser’s own interest ahead of their client’s. Where an SEC registered investment adviser has assumed the authority to vote on behalf of its client, the SEC would require the investment adviser, among other things, must [sic] have a reasonable understanding of the client’s objectives and must make voting determinations that are in their [sic] best interest.¹⁵

The Department acknowledges that, under the Proposed Amendments, “responsible fiduciaries might increase their demands for asset managers to implement separate policies customized for particular ERISA plans or for ERISA plans generally”¹⁶ and requests comment on whether customized policies could benefit plans or increase plan costs.¹⁷

Many investment advisers use consistent proxy voting policies across client accounts, including accounts held by ERISA plans and pooled investment vehicles, because they believe that those policies are in the best interest of their clients.¹⁸ To the extent that the Proposed Amendments would require investment advisers to develop customized voting policies for

¹⁴ 85 FR at 55234.

¹⁵ 85 FR at 55234-55235 (footnote omitted).

¹⁶ 85 FR at 55235.

¹⁷ *Id.*

¹⁸ This should not be surprising considering that most proxy votes relate to routine, uncontested matters. Even for contested matters, an investment adviser may reasonably determine that voting consistently on behalf of ERISA clients and other clients is in the best interest of both categories of clients. Regarding pooled investment vehicles, if the Department proceeds with the Proposed Amendments, we suggest that the Department delete Proposed Rule 404a-1(e)(4)(ii) and amend the beginning of Proposed Rule 404a-1(e)(4)(i)(B) to add the following language in italics: “Where the authority to manage plan assets has been delegated to an investment manager pursuant to section 403(a)(2), *including an investment manager with respect to a pooled investment vehicle that includes plan assets*, the investment manager has exclusive authority to vote proxies or exercise other shareholder rights appurtenant to such plan assets in accordance with this section,....” These amendments would better reflect proxy voting by investment managers with respect to pooled investment vehicles.

particular ERISA plans or collective investment trusts used by ERISA plans, that requirement would certainly increase costs for plans and investment advisers without incremental benefit to participants and beneficiaries.

The Proposed Amendments also establish detailed recordkeeping requirements including that the fiduciary maintain records “that demonstrate the basis for particular proxy votes and exercises of shareholder rights.”¹⁹ For a fiduciary that employs a third party, such as an investment manager or proxy advisory firm, the fiduciary would have to require the third party “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.”²⁰ We discuss above our concerns regarding the “economic benefit” criterion. In addition, to the extent that fiduciaries and their service providers would be required to maintain information in addition to information that they currently retain regarding proxy voting, these proposed requirements would substantially increase costs for fiduciaries and plans and would provide minimal, if any, incremental benefits to participants and beneficiaries.²¹

Given the lack of clarity and substantial burdens on proxy voting in the Proposed Amendments, investment advisers that currently undertake proxy voting on behalf of their ERISA clients may decide to stop providing this service to avoid potential breaches in this area. This would certainly increase costs for plans and provide little, if any, benefit to participants and beneficiaries.

The Proposed Permitted Practices Would Not Ease Compliance Burdens for Fiduciaries

The Department acknowledges that the proposed determination of economic value “may often burden fiduciaries out of proportion to any potential benefit to the plan”²² and it proposes

¹⁹ Proposed Rule 404a-1(e)(2)(ii)(E). The Preamble and the Proposed Amendments refer in several places to voting proxies or exercising “other shareholder rights.” The focus of the rulemaking is clearly on proxy voting and the use of third parties in connection with proxy voting. If the Department proceeds with this rulemaking, it should clarify that the rulemaking refers to proxy voting and not other activities such as corporate actions that are typically addressed by portfolio managers. If the Department intends for the rulemaking to apply to other specific activities, it should explain as much and request comment before proceeding.

²⁰ Proposed Rule 404a-1(e)(2)(iii).

²¹ See page 8 for a discussion of the use of proxy advisory firms by investment advisers and the SEC’s regulation in this area.

²² 85 FR at 55225 (footnote omitted).

“permitted practices” that are designed to “help fiduciaries more cost-effectively comply”²³ with the obligation to vote or not vote. We are concerned, however, that, as proposed, the permitted practices would not ease compliance burdens for plan fiduciaries. The introductory language to the permitted practices provision provides that, “[i]n deciding whether to vote a proxy pursuant to paragraphs (e)(3)(i) and (ii) of this section, plans may adopt proxy voting policies that voting authority shall be exercised pursuant to specific parameters reasonably designed to serve the plan’s economic interest.”²⁴ This language does not provide relief from complying with the requirements of paragraphs (e)(3)(i) and (ii), so it is not clear what advantage would be provided to a fiduciary using a permitted practice.

Even if the Department made clear that fiduciaries using the permitted practices would not be subject to certain provisions of the rule, fiduciaries would still have significant compliance burdens relating to certain permitted practices. For example, the first permitted practice, voting in accordance with management, reads as follows:

A policy of voting proxies in accordance with the voting recommendations of management of the issuer on proposals or particular types of proposals *that the fiduciary has prudently determined are unlikely to have a significant impact* on the value of the plan’s investment, *subject to any conditions determined by the fiduciary as requiring additional analysis* because the matter being voted upon may present heightened management conflicts of interest or is likely to have a significant economic impact on the value of the plan’s investment.²⁵

A fiduciary using this permitted practice would still have to determine whether each proposal has a significant impact on the value of the plan’s investment, and, if it does, whether any conditions require additional analysis. The permitted practice also raises the issue that we discuss above regarding situations where a stock may be held by a plan through multiple fiduciary investment managers. It is not clear how using this permitted practice would help the fiduciary to more cost-effectively comply with the Proposed Amendments. A fiduciary should not be required to analyze the economic impact, or determine conditions for additional analysis, of each proxy vote that is voted using a permitted practice. If the Department proceeds with this rulemaking and wants to provide relief for fiduciaries, the use of a permitted practice should be a clear safe harbor, such as in situations where a plan’s shares are voted pursuant to a written proxy voting policy that is reasonably designed to ensure that shares are voted in the best interest of the plan.

²³ 85 FR at 55225.

²⁴ Proposed Rule 404a-1(e)(3)(iii).

²⁵ Proposed Rule 404a-1(e)(3)(iii)(A) (emphasis added).

Investment Advisers Use Proxy Advisory Firms for a Variety of Important Services

One of the concerns raised by the Department is that “responsible fiduciaries may sometimes rely on third-party advice without taking sufficient steps to ensure that the advice is impartial and rigorous.”²⁶ The Proposed Amendments include provisions that apply to the use of proxy advisory firms by plan fiduciaries. We believe it is important to emphasize the range of valuable services provided by proxy advisory firms. Investment advisers use proxy advisory firms for a number of significant administrative services, such as voting mechanics, data tracking and aggregation, and workflow management. These administrative services are critically important for advisers that manage hundreds, if not thousands, of proxy votes each year. Advisers would need to use these services even if they voted fewer proxies. The Department should not make these services more expensive or difficult to access.

SEC-registered investment advisers are subject to a robust regulatory framework designed to ensure that they conduct appropriate due diligence on third-party providers, including proxy advisory firms.²⁷ The SEC has provided guidance to investment advisers on retaining and overseeing proxy advisory firms, including reviewing conflicts of interest.²⁸ In addition, as the Department noted, the SEC has taken recent actions related to proxy voting, including adopting a rule regarding proxy advisory firms.²⁹ We believe that, rather than proposing regulations regarding the use of proxy advisory firms, the Department should align its approach with that taken by the SEC so that SEC-registered investment advisers are subject to a consistent standard regarding their use of proxy advisory firms. At a minimum, the Department should wait until the implementation of the SEC’s new regulations to determine if any further action is necessary.

Conclusion

For the reasons discussed above, we have very serious concerns about this rulemaking and do not believe that the Department should proceed with it. If the Department believes that it needs to take action in this area, however, we would not object to it making clear that fiduciaries are not required to vote every proxy, and that a fiduciary should have a written proxy voting policy that is reasonably designed to ensure that proxies are voted in the best interest of the plan,

²⁶ 85 FR at 55228.

²⁷ See note 3 regarding SEC regulation of investment adviser proxy voting. We note that, while we are concerned that recent SEC actions may make it more difficult for investment advisers to vote proxies, we believe that the Proposed Amendments would make proxy voting even more challenging for investment advisers that serve ERISA plans.

²⁸ See SEC 2019 Guidance and SEC 2020 Guidance.

²⁹ See note 5.

its participants, and beneficiaries. We do not believe that additional action by the Department regarding proxy voting is necessary or justified by the evidence.

If the Department insists on going forward with this rulemaking, it should provide a substantial transition period of at least 12 months³⁰ to allow plans and fiduciaries to consider what updates are needed to their proxy voting process and the assignment of proxy voting responsibilities. Any updates could require investment advisers to send communications to plan clients and proxy advisory firms, and potentially amend agreements, documentation, and policies and procedures in order to comply with any new requirements.

* * *

We appreciate the Department's consideration of our comments and would be happy to provide any additional information that may be helpful. Please contact Sarah Buescher, IAA Associate General Counsel, or the undersigned at (202) 293-4222 if we can be of further assistance.

Respectfully Submitted,

/s/ Gail C. Bernstein

Gail C. Bernstein
General Counsel

³⁰ We note that the SEC's recent rulemaking that applies to proxy advisory firms has a compliance date of December 1, 2021. We request that the compliance date for this rulemaking be no earlier than that date.