



Will Hild and Beau Brunson
Consumers' Research
1801 F Street, NW
Washington, DC 20006
(202) 898-0542
whild@consumersresearch.org

October 5, 2020

By electronic delivery to:
<http://regulations.gov>

Jason A. DeWitt
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

Consumers' Research Comment to the Department of Labor, Employee Benefits Security Administration on EBSA-2020-0008-0001, Fiduciary Duties Regarding Proxy Voting and Shareholder Rights

Consumers' Research¹ is a 501(c)(3) educational non-profit organization that advocates for the general interests of consumers. This comment letter is intended to present a consumer-focused discussion of the issues relating to the proposal (Proposal) by the Department of Labor (DOL) under Title I of the Employee Retirement Income Security Act of 1974 (ERISA) to amend the "investment duties" regulation at 29 CFR 2550.404a-1 and address the application of ERISA's fiduciary duties of prudence and loyalty to the exercise of shareholder rights, including proxy voting, proxy voting policies and guidelines, and the selection and monitoring of proxy advisory firms.

Because proxy voting is a common practice in both defined benefit (DB) and defined contribution (DC) plans, Consumers' Research applauds the DOL's efforts to clarify the fiduciary duty of proxy voters for retirement plans covered under ERISA. If finalized, the Proposal would clarify the requirement of fiduciaries to exercise shareholder rights, including the voting of proxies, prudently and solely in the economic interests of the plan participants and beneficiaries.

Notably, among other obligations, the Proposal requires these fiduciaries to "[a]ct solely in the economic interest of the plan and its participants and beneficiaries considering only factors that they prudently determine will affect the economic value of the plan's investment."² Moreover, the interests of participants and beneficiaries in their retirement income or financial benefits must be superior to "non-pecuniary" objectives.³

¹ Founded in 1929, Consumers' Research is the nation's oldest consumer affairs organization. Consumers' Research aims to increase the knowledge and understanding of issues, policies, products, and services of concern to consumers and to promote the freedom to act on that knowledge and understanding.

² The Proposal: <https://beta.regulations.gov/document/EBSA-2020-0008-0001>

³ *Id.*

As noted in our comment on DOL RIN 1210-AB95, Financial Factors in Selecting Plan Investments, the exercise of shareholder rights in pursuit of investments that cannot be quantified violates the fiduciary duty of those exercising those rights.⁴ In that comment, Consumers' Research focused on the conflict between the obligations of plan fiduciaries and pressure for investments in line with environmental, social and governance (ESG) goals:

Since there is no consensus on what qualifies as an ESG investment, nor is it possible to quantify the value of an ESG investment monetarily, using ESG considerations as a general guide to investment decisions for retirement plans covered by ERISA is a violation of fiduciary duty. Any fiduciary decision-maker applying ESG metrics to investing does so under his or her personal views, skewed by beliefs and prejudices. In worst-case scenarios, using ESG metrics could even be used to boost interests of decision-makers, rather than clients' interests.⁵

Given the Proposal's clarification that non-pecuniary objectives must not be prioritized above retirement income or financial benefits, we note that ESG-driven and other investments should be pursued only when they can be quantified to demonstrate improved retirement income or financial benefits.

We reiterate this position and welcome the DOL's efforts to align proxy voting with the fiduciary duty of plan investors to focus solely on the financial health of underlying plan assets when voting their shares. In an effort to support the DOL's goal of providing clarity, we appreciate the opportunity to offer some suggestions to bolster the Proposal.

Addressing Proxy Voting Abstentions:

The DOL's stated goal is to prohibit proxy voting without economic due diligence. In order to achieve this objective without the risk of significantly increasing abstentions, the DOL should provide additional clarity with respect to how asset managers should determine whether voting a shareholder action is required due to an action's economic significance. Paragraph (e)(4)(ii) of the proposed rule could be interpreted as requiring abstentions on shareholder actions that are not economically significant to the plan.

Paragraph (e)(4)(ii) reads:

An investment manager of a pooled investment vehicle that holds assets of more than one employee benefit plan may be subject to an investment policy statement that conflicts with the policy of another plan. Compliance with ERISA section 404(a)(1)(D) requires the

⁴ <https://consumersresearch.org/consumers-research-comment-to-the-department-of-labor-employee-benefits-security-administration-on-rin-1210-ab95-financial-factors-in-selecting-plan-investments/>

⁵ *Id.* at 3.

investment manager to reconcile, insofar as possible, the conflicting policies (assuming compliance with each policy would be consistent with ERISA section 404(a)(1)(D)). In the case of proxy voting, to the extent permitted by applicable law, the investment manager must vote (or abstain from voting) the relevant proxies to reflect such policies in proportion to each plan's economic interest in the pooled investment vehicle. Such an investment manager may, however, develop an investment policy statement consistent with Title I of ERISA and this section, and require participating plans to accept the investment manager's investment policy, including any proxy voting policy, before they are allowed to invest. In such cases, a fiduciary must assess whether the investment manager's investment policy statement and proxy voting policy are consistent with Title I of ERISA and this section before deciding to retain the investment manager.

Within the "Regulatory Impact – Vote Category" section, the Proposal states:

If an investor is unsure about a matter or unsure whether her interests and management's interests are aligned, the investor arguably should abstain. The Department requests comments on how often this alignment of interests might occur, and on whether additional direction on voting, such as on the distinction between not voting and abstaining, would be beneficial to fiduciaries.

Consumers' Research believes that, as written, the Proposal will likely lead to substantially more voting abstentions of plan managers and their proxy voters. These abstentions, justified by citing increased costs, probably will impact actions that are likely, but unproven quantitatively, to be economically significant to the plan.

We believe that the DOL should not encourage abstentions. Shareholder proposals are almost always precatory and proposed most often by proponents who have at best only speculative justifications of the economic significance of their proposals to the company. Many such precatory proposals are submitted by shareholders who have motives other than the economic best interests of the corporation, much less other shareholders, at heart. In some years, individuals and institutions have submitted proposals to scores of companies while holding only the bare minimum of stock to meet the submission threshold set by the SEC. As the SEC has found, this "gaming of the system" does not necessarily benefit the economic interests of shareholders as a whole, much less the beneficiaries of ERISA funds in particular.

An increase in the number of abstentions by ERISA fiduciaries whose statutory mandate is to advance and protect the economic best interests of their beneficiaries could have the effect of augmenting the apparent support of such non-economically justified, niche precatory

proposals because abstentions do not always count as a vote not in support of a proposal. As the Proposal states in the “Vote Categories” discussion of Section 1.7 “Uncertainty”:

Broker-dealers may have discretionary authority to vote proxies without receiving voting instructions from the owner of the shares for routine and noncontroversial matters, such as the ratification of a company's independent auditors. For matters in which a broker-dealer does not have discretionary authority to vote, a broker non-vote is required. For matters that require approval of a majority of shares present and voting, abstentions (which are cast neither for nor against a proposal) and broker non-votes are not counted in the final tally. For matters that require approval of a majority of the shares issued and outstanding, abstentions or broker-non votes are treated as votes against the proposal.⁶

Instead of acting as a shield against economically damaging shareholder actions, the Proposal could inadvertently increase the possibility that such actions might be adopted, or at least receive a greater percentage of support than actually is the case because, in matters requiring approval of shares present and voting, the abstentions would not be included in the denominator of the fraction of votes in favor out of total votes present and voting.

In 2014, the SEC staff of the Investment Management and Corporation Finance Divisions in Staff Legal Bulletin No. 20⁷ advanced a solution that makes much sense in the context of these precatory shareholder proposals that have little economic significance for public companies (other than speculative effect). The SEC staff suggested that an investment advisor and its client may take a cost-benefit approach to proxy voting by agreeing that “the time and costs associated with the mechanics of voting proxies with respect to certain types of proposals or issuers” may not serve the best economic interests of the client. In such a case, one approach that the SEC staff posited is that the advisor and its client could agree that the advisor should vote “as recommended by management of the company ... absent a contrary instruction from the client” or absent a determination otherwise by the advisor that other reasons (such as investment strategy) would dictate a different result.

We suggest that this logical, no-nonsense cost-benefit approach would be appropriate for most ERISA funds, particularly if the ERISA fiduciary is satisfied with the issuer’s performance. The SEC staff’s approach also takes into account that a cost-benefit analysis need not be performed each time with regard to the voting of particular precatory shareholder proposals, but generically and programmatically as to the type of proposals and issuers. This model

⁶ Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 55219 at 55235.

⁷ Div. of Investment Management and Div. of Corp. Finance, U.S. Securities and Exchange Commission, “Proxy Voting: Proxy Voting REsponsibilities of Investment Advisers and Availability of Exemptions from the Proxy Rules for Proxy Advisory Firms,” Staff Legal Bulletin No. 20 (June 20, 2014), https://www.sec.gov/interps/legal/cfslb20.htm#_ftnref2

would be appropriate for ERISA managers, and we recommend that the DOL adopt such an approach.

Enhanced Clarity Regarding Economic Impact:

Paragraph (e)(2)(ii) delineates the primary elements of the Proposal relating to DB and DC plans. In subsections D through F, the DOL provides asset managers with easy to understand requirements should they want to employ proxy voters. On the other hand, subsections A through C set forth the fiduciary requirements for asset managers to meet the threshold of “act[ing] solely in accordance with the economic interest of the plan,” but those subsections lack the clarity of subsections D through F.

Paragraph (e)(2)(ii) reads:

In order to fulfill the fiduciary obligations under paragraph (e)(2)(i) of this section, when deciding whether to exercise shareholder rights and when exercising shareholder rights, a plan fiduciary must:

(A) Act solely in accordance with the economic interest of the plan and its participants and beneficiaries considering only factors that they prudently determine will affect the economic value of the plan’s investment based on a determination of risk and return over an appropriate investment horizon consistent with the plan’s investment objectives and the funding policy of the plan;

(B) Consider the likely impact on the investment performance of the plan based on such factors as the size of the plan’s holdings in the issuer relative to the total investment assets of the plan, the plan’s percentage ownership of the issuer, and the costs involved;

(C) Not subordinate the interests of the participants and beneficiaries in their retirement income or financial benefits under the plan to any non-pecuniary objective, or sacrifice investment return or take on additional investment risk to promote goals unrelated to those financial interests of the plan’s participants and beneficiaries or the purposes of the plan;⁸

With respect to subsections A through C, the DOL should consider clarifying what actions plan managers need to take to meet the DOL’s requirements for exercising shareholder rights. While such additional clarity could have an impact on the flexibility given to asset managers, enhanced regulatory certainty would ensure that their responsibilities do not become more vague and thus more open to unwarranted liability over time.

⁸ Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 55219 at 55242.

Potential Improvements to Cost/Benefit Analysis:

The DOL has taken considerable steps to provide a robust cost/benefit analysis of the Proposal. However, in the “Uncertainty – Cost Savings” section of the Proposal, the DOL draws particular attention to a lack of underlying data. The pertinent section states:

As noted earlier, the Department currently lacks complete data on plans’ exercise of their shareholder rights appurtenant to their stock holdings, including proxy voting activities, and on the attendant costs and benefits. The Department invites comments that illuminate these activities, including their costs and benefits, as well as comments regarding how this proposal would change these activities.⁹

Consumers’ Research agrees with the DOL that the lack of comprehensive data adds uncertainty to the Proposal; however, this lack of data does not weaken the Proposal. Rather, it highlights the necessity for plan managers or their proxy advisory firms to perform and provide robust economic analysis before voting proxies. Plan managers and proxy advisory firms should have all underlying data necessary to perform the required analysis.

It is unquestionable that voting decisions must be made in accordance with the fiduciary duty set forth under ERISA. As such, expanding economic analysis to include all decisions would likely impose a minimal burden on plan managers or proxy advisors. In order to ensure that the rule does in fact impose a minimal burden on plan managers and proxy advisory firms, the DOL could allow these firms to make the data used for voting shareholder decisions publicly available for external economic analysis. This approach would allow academics, think tanks, and concerned citizens to provide additional robust economic analysis.

To ensure the best possible outcome for consumer investors, the DOL may find it beneficial in a final rule to issue guidelines for how plan managers and proxy advisors can release aggregate shareholder data stripped of any proprietary Personally Identifiable Information for use in public economic analysis. The DOL should base its guidelines on the Federal Government’s Open Data Policy.¹⁰ As noted in the Proposal, robust economic analysis is required by Executive Order 12866¹¹ for all major proposed rules. Consumers’ Research believes that allowing the general public to provide additional data analysis after the release of anonymized aggregate shareholder data would meet both the letter and spirit of Executive Order 12866.

⁹ *Id.* at 55233.

¹⁰ <https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/memoranda/2013/m-13-13.pdf>

¹¹ <https://www.archives.gov/files/federal-register/executive-orders/pdf/12866.pdf>

Conclusion:

Consumers' Research believes the DOL's Proposal on proxy voting is well-intentioned and provides much needed clarity on the fiduciary requirements for plan managers and proxy advisors. Moreover, we appreciate the DOL's request for comments relating to key areas where the DOL has acknowledged the need for input, including regarding costs and benefits. The overall goal of requiring plan managers and proxy voters only to take economic considerations into account when voting a shareholder action is in the best interest of consumer investors. Consumers' Research is confident that, with further clarification, the DOL will successfully meet its objectives of addressing areas of misunderstanding that linger from sub-regulatory guidance and letters issued in past years and, ultimately, issue an improved investment-duties regulation.

Sincerely,

Will Hild

Will Hild, Executive Director

Beau Brunson

Beau Brunson, Policy Director