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Employee Benefits Security Administration  
U.S. Department of Labor  
200 Constitution Avenue, NW  
Washington, DC 20210

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Docket RIN 1210-AB79  
Docket Number: EBSA-2020-0008

## Re: Proposed Rule on Fiduciary Duties Regarding Proxy Voting and Shareholder Rights

ASHLEY BAKER  
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THE COMMITTEE FOR JUSTICE

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### INTRODUCTION

We at the Committee for Justice (“CFJ”) respectfully address the Department of Labor regarding its request for public comment on its proposed rule on proxy voting.<sup>1</sup>

Founded in 2002, CFJ is a nonprofit legal and policy organization that promotes and educates the public and policymakers about the rule of law and the benefits of constitutionally limited government. CFJ has recently focused on issues at the intersection of constitutional law and regulatory reform. Consistent with that mission, our latest efforts have encompassed areas such as intellectual property law, antitrust law, privacy law and policy, and administrative law.<sup>2</sup>

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<sup>1</sup> U.S. Department of Labor, Proposed Rule on Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, Docket RIN 1210-AB79 (Sept. 4, 2020), <https://www.federalregister.gov/documents/2020/09/04/2020-19472/fiduciary-duties-regarding-proxy-voting-and-shareholder-rights>

<sup>2</sup> See, e.g. Ashley Baker, Comments Submitted to the FTC Regarding Hearings on Competition and Consumer Protection in the 21st Century, Docket No. FTC-2018-0098. (Dec. 2018), [https://www.ftc.gov/system/files/documents/public\\_comments/2018/12/ftc-2018-0098-d-0033-163368.pdf](https://www.ftc.gov/system/files/documents/public_comments/2018/12/ftc-2018-0098-d-0033-163368.pdf); Ashley Baker, Comments Submitted to the DOJ Antitrust Division Regarding Competition in Television and Digital Advertising. June 2019, <http://bit.ly/2PwehnJ>.



In comments filed earlier this year, we expressed our view that the Securities and Exchange Commission's proposed rule change<sup>3</sup> regarding proxy advisory firms is a positive step towards implementing much-needed reforms. The rules governing the proxy system need to be clarified and modernized for the benefit of investors, public companies, and the U.S. financial services industry as a whole.

We believe that Department's proposed rule is a strongly positive step, clarifying and modernizing regulations on proxy voting. The proxy environment has changed dramatically in recent years as the proportion of institutional ownership has increased, activists have flooded issuers with proxy proposals, and ESG investing has come into vogue. In addition, as the Department points out, the current regulatory regime on proxy voting is often unclear, especially following such guidance as the Avon Letter.

## THE INTERESTS AND PRIORITIES OF PROXY FIRMS – AND ADVISORS' DEFERENCE TO THEM – ARE OUT OF KEEPING WITH THE LEGAL STANDARDS GOVERNING THE REST OF THE FINANCIAL SERVICES INDUSTRY

When they rely on recommendations from proxy advisory firms, pension plan advisors may not be fulfilling their proper fiduciary duties. As a report by the Manhattan Institute explained:<sup>4</sup>

“Proxy advisory firms are not held to a fiduciary standard that would require them to demonstrate that their recommendations are in the best interest of shareholders and the corporation— or, at least, no such standard that has been clearly articulated in rules or regulations or litigated in a court of law. This absence of fiduciary duties is salient, given the evidence that at least some institutional investors use proxy advisory firms as a lowest-cost option to meet their own fiduciary voting obligations, without regard to voting accuracy.”

In its proposed rule, the Department makes it clear that simple reliance on proxy advisory firms is not enough for pension plan advisors to fulfill their duty to clients under ERISA. The rule states

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<sup>3</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), <https://www.sec.gov/rules/proposed/2019/34-87457.pdf>.

<sup>4</sup> James R. Copeland, David F. Larcker, & Brian Tayan, Proxy Advisory Firms: Empirical Evidence and the Case for Reform, The Manhattan Institute, (May 2018), <https://media4.manhattan-institute.org/sites/default/files/R-JC-0518-v2.pdf>.



that pension fiduciaries must “investigate material facts that form the basis for any particular proxy vote or other exercise of shareholder rights (e.g., the fiduciary may not adopt a practice of following the

Recommendations of a proxy advisory firm or other service provider without appropriate supervision and a determination that the service provider’s proxy voting guidelines are consistent with the economic interests of the plan and its participants and beneficiaries.”

The proposed rule only briefly addresses the most egregious example of fiduciaries’ outsourcing their decisions to proxy advisory firms – the practice of “robo-voting,” or voting in lockstep with advisory firms, often using pre-populated ballots. The Department should simply ban this practice because it clearly does not meet the requirements of “appropriate supervision” and voting “with the economic interests of the plan” or with the need to “investigate material facts.”

Smaller plans sometimes engage in the practice of robo-voting because they don’t have the resources to process thousands of proposals each year. The Department has made clear that an acceptable alternative for these plans is not voting at all if the costs exceed economic – as opposed to ancillary or non-pecuniary benefits.

Notably, proxy advisory firms may have political and ideological agendas that present conflicts. Glass Lewis and ISS, by far the largest such firms, often give guidance promoted by ESG advocate even though this type of corporate strategy does not necessarily produce the best returns for investors, as you show in your proposed rule. The only goal for a pension fiduciary must be to maximize return on investment (ROI). For ISS and Glass Lewis, ROI can take a backseat to non-pecuniary interests.

## **PROXY ADVISORY FIRMS SHOULD NOT BE PERMITTED TO HAVE FINANCIAL RELATIONSHIPS WITH ISSUERS**

Proxy advisory firms cannot possibly serve the interests of both issuers and investors at the same time, yet some of these firms, notably ISS, continue to provide corporate-governance consulting services to some of the same companies for which they offer voting recommendations.



As Glass Lewis stated in a letter to the Senate Banking Committee, “unlike ISS, Glass Lewis does not provide consulting services to issuers. We believe the provision of consulting services creates a problematic conflict of interest that goes against the very governance principles that proxy advisors like ourselves advocate.”<sup>5</sup> Indeed, conflicts that would be material should be prohibited.

The ownership of proxy advisory firms presents another conflict. Glass Lewis is jointly owned by the Ontario Teacher’s Pension Board and a hedge fund, Alberta Investment Management Corporation. ISS is owned by private equity firm Genstar Capital. These investment firms have a stake in the issuers that proxy recommendations by ISS and Glass Lewis. Therefore, the ownership entities must disclose those conflicts.

## PROXY ADVISORS FIRMS PRESENT AN AGENCY PROBLEM

If an individual investor wants to invest in stocks to promote environmental or social objectives, that is her right. But a pension plan is a different matter. A pension fiduciary must make decisions in the interest of increasing risk-adjusted returns for beneficiaries. The same is true for proxy advisory firms, which also act as agents.

While there is anecdotal evidence of the concerns of investors in the many public comments submitted to the Department, a recent study provides reliable data on the matter.<sup>6</sup> In November 2019, the financial research firm Spectrem conducted a survey of more than 5,000 investors who hold at least \$10,000 in assets through various accounts containing stocks, bonds, mutual funds and exchange-traded funds (ETFs).<sup>7</sup> The findings were as follows:

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<sup>5</sup> Glass Lewis, Letter to the Senate Banking Committee, (May, 9 2018), [http://www.glasslewis.com/wp-content/uploads/2018/06/Glass-Lewis-Response-to-May-9-2018-Chairman-Heller-Letter\\_0601\\_FINAL.pdf](http://www.glasslewis.com/wp-content/uploads/2018/06/Glass-Lewis-Response-to-May-9-2018-Chairman-Heller-Letter_0601_FINAL.pdf)

<sup>6</sup> Tom Zanki, Law360, (January 9, 2020), <https://www.law360.com/compliance/articles/1232829/survey-says-retail-investors-want-more-proxy-firm-scrutiny>.

<sup>7</sup>Press Release, Spectrem Group Study Reveals Wide Retail Investor Support for Proposed SEC Amendments, PR Newswire, (Jan. 10, 2020), <https://www.prnewswire.com/news->



- **Increased Scrutiny:** 81% of retail investors support more scrutiny of proxy firms.
- **Conflicts of Interest:** 78% of retail investors support requiring proxy firms to disclose conflicts of interest
- **Robo-voting:** 81% of survey respondents said they were concerned about robo-voting (notably, 35% said they're "very concerned")

Equally important, the survey found that 91% of retail investors "indicated a preference for wealth maximization over political or social objectives."<sup>8</sup>

## CONCLUSION

With the changes we suggest, the Department's proposal deserves considerable praise. It helps ensure that fiduciaries perform their proper duty of maximizing returns for current and future retirees, using a disclosure-based regulatory framework. Smart regulation of this nature boosts the U.S. economy for the benefits of all Americans.

Fundamentally, the Department should strengthen its proposed rule by specifying oversight over robo-voting. All asset managers, including private pension fund managers, should not be permitted to take part in robo-voting especially since it should not be compliant with the Department's objective for an investigation of material facts. The practice of automatic robo-voting would be incompatible with this aspect of the rule that requires due diligence and investigation by plan managers.

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[releases/spectrem-group-study-reveals-wide-retail-investor-support-for-proposed-sec-amendments--january-10-2020-300984956.html](https://www.spectrem.com/Content/Press/press-release-new-spectrem-study-reveals-significant-concern-among-retail-investors-over-role-of-proxy-advisors.aspx).

<sup>8</sup> Press Release, New Spectrem Group Study Reveals Significant Concern Among Retail Investors Over Role Of Proxy Advisors, (April 2, 2020), <https://www.spectrem.com/Content/Press/press-release-new-spectrem-study-reveals-significant-concern-among-retail-investors-over-role-of-proxy-advisors.aspx>