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The Forum for Sustainable and Responsible Investment

Submitted via regulations.gov

October 5, 2020

Joe Canary
Office of Regulations and Interpretations
US Department of Labor
Room N-5655
200 Constitution Avenue NW
Washington, DC 20210

RE: Proposed rule on Fiduciary Duties Regarding Proxy Voting and Shareholder Rights (RIN 1210-AB91)

Dear Mr. Canary:

I write to provide comments in response to the Department of Labor's proposed rule, "Fiduciary Duties Regarding Proxy Voting and Shareholder Rights" (RIN 1210-AB91) (the "Proposal"). The Proposal does not describe a sufficient rationale to support changes to proxy voting. Further, the limitations placed upon proxy voting show a clear desire to shift power from investors to company management and to ensure that such management hears as little as possible from fiduciaries. We were not aware that this was the role of the Department of Labor. The Proposal should be withdrawn.

US SIF: The Forum for Sustainable and Responsible Investment is the leading voice advancing sustainable investing across all asset classes. Our mission is to rapidly shift investment practices toward sustainability, focusing on long-term investment and the generation of positive social and environmental impacts. Our members, comprised of investment management and advisory firms, mutual fund companies, asset owners, research and data firms, financial planners, advisors and broker-dealers, represent more than $3 trillion in assets under management or advisement. US SIF members integrate environmental, social and governance factors ("ESG") into their investment decisions and take their responsibilities seriously as shareowners, including voting proxies and engaging with companies.

Summary

On August 31st, the Department of Labor announced[1] a proposed rule directed at proxy voting by fiduciaries of ERISA-governed retirement plans. The Proposal's intent appears to be to

[1] Department of Labor press release, "U.S. Department of Labor Proposes Rule on Employee Benefit Plan Proxy Voting and Exercises of Other Shareholder Rights;" (August 31, 2020). https://www.dol.gov/newsroom/releases/ebsa/ebsa20200831

reduce proxy voting, especially on environmental and social issues. It sets up a dynamic where ERISA-governed funds will be encouraged not to vote most proxies.

While purporting to clarify duties pertaining to proxy voting, the Proposal: 1) establishes onerous obligations on fiduciaries to demonstrate a proxy vote's "expected economic benefit" to the plan for any vote that departs from management's recommendations, 2) includes an explicit ban on proxy voting where economic benefit cannot be demonstrated or when the economic benefit is too small to impact plan performance and 3) proposes safe harbor provisions that seek to dissuade fiduciaries from voting, and if they do vote, to vote with management or abstain from voting.

In 2016, the DOL issued guidance (IB-2016-01) that stated that voting proxies and shareholder engagement were consistent with fiduciary duty, assuming that the practices had a reasonable expectation of positive impact on the plan after taking expenses into account. The new Proposal would override the 2016 guidance. If finalized, the Proposal will give DOL regulatory enforcement mechanisms that currently do not apply to IB-2016-01 department guidance.

The Proposal does not demonstrate a rationale for the suggested changes. The Proposal also reflects a fundamental misunderstanding of the importance fiduciaries and other investors place on voting proxies in order to communicate their preferences to company management and other shareowners. Without this channel of communication, the investor voice is greatly diminished.

Shareholder voting matters

One of the fundamental rights of owning shares is the right to vote a proxy.[2] It is wrong for the DOL to tell a fiduciary they should not exercise their right to vote. Such disenfranchisement is fundamentally inappropriate.

The Proposal restricts the right to vote in paragraph (e)(3)(ii), "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..."[3]

Shareholders' voting rights are granted by state corporate law[4] and, in the case of say-on-pay, through federal legislation.[5] The DOL does not offer any good reason to supplant the considered judgment of experienced plan fiduciaries with its own judgment of when shareholders should be voting.

Proxy voting is one of the most visible and verifiable ways in which investors can practice responsible ownership. A key element of proxy voting is allowing shareholders to raise issues before a crisis that erodes shareholder value occurs.

Academics have studied the impact of proxy voting and concluded:

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[2] The Modern Corporation and Private Property. By Adolf A. Berle, Jr. and Gardiner C. Means. New York: The Macmillan Company, 1932.
[3] "Fiduciary Duties Regarding Proxy Voting and Shareholder Rights," Proposed Rule ("Proposal"); Federal Register, Vol. 85, No. 173 (Friday, September 4, 2020).
[4] "Shareholder rights and powers in USA," Sidley Austin LLP (July 10, 2018) https://www.lexology.com/library/detail.aspx?g=1b53f42b-40df-420e-a54f-8cf522990345
[5] Dodd–Frank Wall Street Reform and Consumer Protection Act §951

> "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."[6]

Further, Goldman Sachs Equity Research found that "shareholder resolution activity can complement the investor mosaic of material and emerging Environmental, Social & Governance (ESG) risks faced by corporates, in addition to measurable performance, incentives and intensities."[7]

Insufficient rationale provided to support changes to proxy voting

The DOL presents no empirical data to support its contention that plan fiduciaries are using excessive plan resources to research and vote proxies. The Proposal cites the Business Roundtable's comment letter to the SEC's Rule 14a-8 rulemaking and the Washington Legal Foundation.[8] Neither of these can be considered independent sources of research or data.

If excessive use of plan resources was a legitimate problem in ERISA-governed plans, DOL should be able to demonstrate the urgent need to regulate proxy voting with specific examples of enforcement actions or litigation against fiduciaries. DOL has failed to produce such evidence.

In fact, current guidance by DOL (IB-2016-01) accurately acknowledges that voting proxies incurs very little expense to the plan:

> 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.[9]

If the cost of proxy voting had significantly changed since IB-2016-01 was issued in late 2016, surely DOL would have provided data to justify the Proposal. It has not.

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[6] Competing for Votes, Nili, Yaron and Kastiel, Kobi, (August 26, 2020). 10 Harvard Business Law Review 287 (2020), Univ. of Wisconsin Legal Studies Research Paper No. 1605.

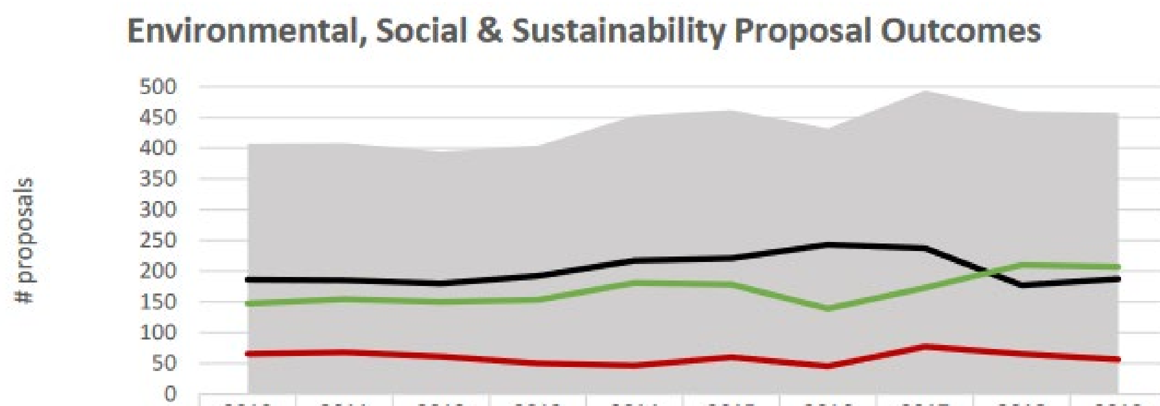
[7] "Shareholder Engagement in the Age of Transparency" Goldman Sachs Equity Research (June 12, 2019), https://www.eticanews.it/wp-content/uploads/2019/06/Shareholder-engagement-in-the-age-of-transparency-1.pdf

[8] Proposal, footnote 12, "Daniel M. Gallagher, Outsized Power & Influence: The Role of Proxy Advisers, Washington Legal Foundation (Aug. 2014), https://s3.us-east-2.amazonaws.com/washlegal-uploads/upload/legalstudies/workingpaper/GallagherWP8-14.pdf, at 3; Business Roundtable Comment Letter on SEC Proposed Amendments to Rule 14a-8 (Feb. 3, 2020), www.sec.gov/comments/s7-22-19/s72219-6742505-207780.pdf, at 2-3 ("many institutional investors historically interpreted SEC and Department of Labor rules and guidance as requiring institutional investors to vote every share on every matter on a proxy") (citing Gallagher).

[9] Interpretive Bulletin 2016-01, Department of Labor (2016)

The DOL alludes that "voting costs sometimes exceeding attendant benefits has been amplified by the recent increase in the number of environmental and social shareholder proposals introduced." In reality, on average, only 13 percent of Russell 3000 companies received a shareholder proposal in any one year between 2004 and 2017. In other words, the average Russell 3000 company can expect to receive a proposal once every 7.7 years.[10]

The Proposal also implies that the number of environmental and social proposals submitted are burdening plan fiduciaries who cast votes.[11] Voting data analyzed by the Sustainable Investments Institute (graph below) shows the number of proposals that go to a vote is largely stable over time.[12] The number of proposals filed has held relatively steady for the past five years or so, and declined since 2017. In 2019, 460 proposals were filed by shareholders, but less than half were on proxy ballots. The remainder were omitted for procedural reasons or through appeals for no-action relief to the SEC or withdrawn. It does not seem onerous or costly for approximately 200 shareholder proposals to be voted upon per year. The DOL has certainly not made a case that it is.



	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
total	407	408	395	404	453	462	432	494	460	457
omitted	65	68	61	50	46	60	45	77	65	56
voted	186	185	180	192	217	221	243	237	177	187
withdrawn	147	154	150	153	181	178	139	173	210	207

Excludes 62 not voted for other reasons, 7 in 2019.
Source: Sustainable Investments Institute (Si2)

The Proposal is onerous and unworkable

[10] CII Letter to Senators Michael Crapo and Sherrod Brown (Dec. 4, 2018), available at https://www.cii.org/files/issues_and_advocacy/correspondence/2018/December%205%202018%20Letter%20to%20Senate%20Banking.pdf

[11] The Proposal states "From 2011 through 2017, shareholders *submitted* 462 environmental proposals and 841 social shareholder proposals, and resubmitted at least once 41 percent of environmental and 51 percent of social proposals." [emphasis added.]

[12] "FACT SHEET: Shareholder Proposal Trends," Sustainable Investments Institute (Si2), (January 28, 2020). https://siinstitute.org/special_report.cgi?id=80

The Proposal's requirement to document the calculations behind each vote is onerous and unworkable. The Proposal will require fiduciaries to calculate the economic impact of every vote on the proxy ballot, including for or against directors, to approve independent auditors as well as say-on-pay and shareholder proposals. This is costly and imprudent use of plan assets – the exact thing DOL should be protecting against.

Paragraph (e)(2)(ii) sets out the obligations for fiduciaries casting a vote. These calculations of economic impact require that fiduciaries "[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." Based upon cost examples DOL included in the Proposal, Glass Lewis found that researching and documenting the required analyses for every individual vote would result in compliance costs of $13 billion a year.[13]

The Proposal's recommendation to counter these extreme costs and analytical burdens is to have fiduciaries adopt "permitted practices."[14] Permitted practices are blanket voting policies that allow fiduciaries to avoid the vote-by-vote cost-benefit analysis prescribed in Paragraph (e)(2)(ii). Three permitted practices are described in the Proposal. The first practice is to vote in alignment with management. The second practice only allows for voting on certain types of proxy ballot items.[15] The third practice requires the fiduciary to "refrain from voting unless they determine they have an economically significant holding in the company such that the vote would have a material impact on plan performance."

However, the permitted practices, in effect, allow plan fiduciaries to vote on matters that may not have economic impact on plan performance if they vote with management. This contradicts the purported primary objective of the Proposal to eliminate voting on proxy proposals that have no economic benefit. There is also an implicit assumption that management's recommendations are always correct. There is ample evidence in the history of corporate bankruptcies, scandals and value collapses that this is not the case. While management's recommendations are often sound, there is no evidence to support the contention that they are always sound.

Further, always voting with management on such questions as the election of directors, executive compensation and the pairing of executives' golden parachutes with corporate mergers may violate the duty of loyalty because of management's own conflicts of interest. The Proposal offers no explanation why voting in alignment with management is in the best interests of plan participants. Voting proxies is important so that management hears the concerns that shareholders have. Recommending that fiduciaries have a policy to vote in line with management guts one of the major reasons for voting proxies.

The Proposal concentrates voting power in a small number of large asset managers

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[13] "Disenfranchising Shareholders and Reducing Corporate Accountability" Glass Lewis (September 21, 2020) https://www.glasslewis.com/disenfranchising-shareholders-and-reducing-corporate-accountability-comments-due-on-dol-proposal-to-limit-shareholder-voting-by-october-5-2020/

[14] Proposal, paragraph (e)(3)(iii)

[15] Permitted types of votes under (e)(3)(iii)(B), "mergers and acquisitions transactions, dissolutions, conversions, or consolidations), corporate repurchases of shares (buy-backs), issuances of additional securities with dilutive effects on shareholders, or contested elections for directors;"

The Proposal could lead to an extreme concentration of voting power among a few large firms whose proxy votes are large enough to “make an economic impact on the plan’s investment.” The onerous requirements to justify proxy voting and the threat of a regulatory investigation into voting practices will likely dissuade many plans from voting. This will leave the fiduciaries of the largest plans, who meet the “economic impact” threshold, with outsized influence and the ability to stifle the voice of others. Such concentration is not good for healthy markets.

In addition, DOL explicitly states that it is only interested in allowing large plan fiduciaries to vote proxies by suggesting that the requisite ownership level be five percent.

> “The Department also believes that determining materiality based on a percentage of plan assets could be a straightforward way for fiduciaries to apply such a cap, and specifically solicits comments on whether in setting this upper limit, the Department should look to financial practices and existing regulations regarding quantitative measures of materiality… In particular, the Department solicits comments on whether a ***five-percent cap*** would be appropriate or some other percent level of plan assets.”[16] [emphasis added]

Owning five percent of companies is only attainable by the largest asset managers who act as plan fiduciaries, though this may not be possible for even the largest firms. For example, owning five percent of Amazon means a position size of $157 billion. A five percent position of Apple means a position size of $100 billion.

The Proposal ignores the value of collective voting among like-minded shareholders. Proxy voting not only allows shareholders to communicate their views to management; it also allows them to communicate with fellow shareholders. DOL would deny the opportunities for smaller voters to join like-minded shareholders to earn a significant vote level to get management’s attention.

Environmental and social issues are material to company performance

Climate change, diversity and workplace discrimination are material long-term systemic risks. They are just a few of the kinds of risks that the DOL glosses over in the dismissal of proposals focused on environmental and social criteria. The Proposal states, “It is likely that many of these proposals have little bearing on share value or other relation to plan interests.”

There is now ample literature that makes clear that ESG criteria are material to long-term shareholder value. For example, the CFA Institute, the leading investment professional standards organization, identifies ESG criteria as financially material: "CFA Institute encourages all investment professionals to consider ESG factors, where relevant, as an important part of the analytical and investment decision-making process, regardless of investment style, asset class, or investment approach."[17]

Two meta-studies arrive at the same conclusion. The first, published by The *Journal of Sustainable Finance & Investment* considered 2,200 individual studies and reported that 90

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[16] Proposal, section C, “Provisions of the Rule”.
[17] Positions on Environmental, Social, and Governance Integration, CFA Institute (2018) https://www.cfainstitute.org/-/media/documents/article/position-paper/cfa-institute-position-statement-esg.ashx

percent of the studies found a non-negative relationship between ESG considerations and corporate financial performance with a clear majority showing a positive relationship.[18] The second, by Oxford University and Arabesque Partners, considered 200 sources and concluded, "88 percent of reviewed sources find that companies with robust sustainability practices demonstrate better operational performance, which ultimately translates into cash flow," and "80 percent of the reviewed studies demonstrate that prudent sustainability practices have a positive influence on investment performance."[19]

In fact, much work over the past decade has established materiality standards for ESG issues. The Sustainability Accounting Standards Board (SASB) and the Global Reporting Initiative (GRI), through multi-stakeholder processes that include corporations, investors and other market participants, have created corporate sustainability reporting standards for ESG issues. Fifty-one percent of the S&P 500 reporting companies use GRI.

Currently, 145 asset managers and asset owners representing more than $53.2 trillion in assets under management participate in SASB's investor advisory group. SASB's Materiality Map is a summary of sustainability issues that are "likely to affect the financial condition or operating performance of companies within an industry." As an example, SASB found climate risk is present in 72 of 79 industries.[20] Prudent fiduciaries cannot ignore these risks when voting proxies.

There are many examples of managerial strategies that could be classified as "ESG failures" and were disastrous for investors and employees: AIG, Bear Stearns, Lehman Brothers, BP, Enron, WorldCom, Fannie Mae and Freddie Mac, Massey Energy, Volkswagen and Wells Fargo. Scandals and disasters are the visible portion of the larger iceberg of incentives that lure corporate managers to manage for the short term and take excessive risk at shareholders' expense.[21]

The Proposal fails to provide a cost-benefit analysis

The absence of a cost-benefit analysis should disqualify the proposed rule. The DOL provides no data to quantify the purported benefits: "The societal resources freed for other uses due to voting fewer proxies (minus potential upfront transition costs) would represent benefits of the rule; in other words, the increased returns would be associated with investments generating higher pre-fee returns, which means the higher returns qualify as benefits of the rule."[22] No analysis is provided for this statement, nor is a numerical benefit calculated. This statement

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[18] ESG And Financial Performance: Aggregated Evidence from More Than 2000 Empirical Studies, Gunnar Friede, Timo Busch, Alexander Bassen, *Journal of Sustainable Finance & Investment* (Volume 5, 2015 – Issue 4) https://www.tandfonline.com/doi/full/10.1080/20430795.2015.1118917

[19] From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance," Gordon Clark, Andreas Feiner, Michael Viehs. University of Oxford and Arabesque Partners. (March 2015) https://arabesque.com/research/From_the_stockholder_to_the_stakeholder_web.pdf

[20] SASB Climate Risk Technical Bulletin TB001-10182016 (October 2016). https://www.sasb.org/wp-content/uploads/2019/08/Climate-Risk-Technical-Bulletin-web.pdf

[21] "The Business Case for the Current SEC Shareholder Proposal Process," Ceres, US SIF, ICCR (April 2017) https://www.ussif.org/files/Public_Policy/Comment_Letters/Business%20Case%20for%2014a-8.pdf

[22] Proposal, section 1.3 "Benefits".

from the DOL can just as easily be understood as departmental preference that companies aren't bothered by shareowners. This is assuredly not the role of the Department of Labor.

This Proposal will disenfranchise fiduciaries from their right to vote, further move power from investors to company management and lessen confidence in the rulemaking role of the Department of Labor.

I respectfully request that the Proposal be withdrawn.

Thank you for your consideration of these comments.

Sincerely,

Lisa N. Woll

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