October 5, 2020

Via Electronic Submission:

Office of Regulations and Interpretations
Employee Benefits Security Administration, Room N-5655
U.S. Department of Labor
200 Constitution Avenue NW
Washington DC, 20210

Re: Fiduciary Duties Regarding Proxy Voting and Shareholder Rights; RIN 1210–AB91

Dear Sir or Madam,

Managed Funds Association ("MFA") and the Alternative Investment Management Association ("AIMA") (the "Associations") appreciate the opportunity to provide comments to the Department of Labor ("DOL") in response to the proposed rule (the "Proposed Rule") regarding the application of the prudence and exclusive purpose duties in the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), with respect to proxy voting and the exercise of other shareholder rights.[1] We support the DOL's efforts to clarify an ERISA fiduciary's duties in this context—specifically, that ERISA fiduciaries are not required to vote all proxies—with the goal of enabling ERISA fiduciaries to focus on activities most likely to have an economic impact on a plan's investments. We also support the DOL's efforts to update its regulations to ensure more consistent requirements applicable to all plan fiduciaries in light of recent actions by the Securities and Exchange Commission ("SEC") related to the proxy voting process.[2] Providing clear and consistent requirements for proxy voting and the exercise of other shareholder rights, without duplicative and unnecessary compliance burdens on ERISA fiduciaries and investment managers that have been delegated proxy voting authority, will reduce costs in managing plan assets and ultimately benefit plan participants and beneficiaries.

We understand the Department's desire to correct a "persistent misunderstanding" that proxy voting is required of ERISA fiduciaries in all circumstances and appreciate that the Release seeks to provide multiple approaches that ERISA fiduciaries can use to determine whether to vote or not vote proxies in accordance with their fiduciary duties. However, we have some concerns that,

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1 Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 55,219 (Sept. 4, 2020) (to be codified at 29 C.F.R. 2550.404a-1) (the "Release").

2 *See* Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, 84 FR 47420 (Sept. 10, 2019) ("2019 SEC Proxy Voting Guidance"); Exemptions from the Proxy Rules for Proxy Voting Advice, SEC Release No. 34-89372 (July 22, 2020); Supplement to Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, SEC Release No. IA-5547 (July 22, 2020).

absent further clarification, the Release may minimize the effectiveness of several of the proposed approaches, which could risk discouraging ERISA fiduciaries from engaging in any proxy voting at all or, alternatively, result in ERISA fiduciaries incurring substantial compliance costs to justify and document the fiduciary's determination of whether and how to vote—costs that will likely be passed on to plan participants and beneficiaries. More specifically, in an effort to avoid the potential liability that is both expressly and impliedly indicated by the Release with respect to proxy voting determinations, we believe that the Proposed Rule could result in many ERISA fiduciaries and investment managers that have been delegated proxy voting authority *increasing* the resources devoted to evaluating, investigating and documenting proxy voting determinations, and supervising service providers, in a manner that is disproportionate to the potential benefits of proxy voting. This result would significantly undermine the DOL's stated objective in issuing the Proposed Rule to ensure that plan fiduciaries only incur costs to vote proxies and exercise other shareholder rights that are economically justified. In adopting a final rule, we urge the DOL to carefully consider both the rule text and structure, and commentary in the adopting release, in order to avoid this outcome.

In this letter, we focus our comments on several key refinements and clarifications that we believe will further the DOL's goals in issuing the Proposed Rule, improve the operation of the Proposed Rule, and avoid imposing unnecessary costs on ERISA fiduciaries and investment managers that have been delegated proxy voting authority.

Specifically, we believe that the DOL should:

- Clarify the interaction of the "permitted practices" set forth in paragraph (e)(3)(iii) of the Proposed Rule with the enumerated obligations set forth in paragraph (e)(2)(ii) of the Proposed Rule. In this regard, the DOL should:
    - clarify that an ERISA fiduciary will be deemed to satisfy the enumerated obligations if the fiduciary votes in accordance with prudently adopted proxy voting policies that are consistent with the "permitted practices";
    - specifically provide in the rule text that ERISA fiduciaries will not be subject to liability for engaging in (or abstaining from) voting proxies in accordance with prudently adopted policies that are consistent with the "permitted practices"; and
    - provide more clarity that an SEC-registered investment adviser that has complied with its fiduciary duty under the Investment Advisers Act of 1940 with regard to proxy voting will satisfy the obligations under the Proposed Rule, as long as its proxy voting policies are consistent with the "permitted practices." If compliance with SEC rules and guidance is insufficient for this purpose, the DOL should more clearly specify what additional actions are required, while seeking to avoid potentially incompatible standards for ERISA fiduciaries and SEC-registered investment managers.
- Clarify that a third-party investment manager would not be subject to specific documentation requirements regarding the basis of any particular proxy vote where the investment manager votes in accordance with prudently adopted proxy voting policies that are consistent with the "permitted practices"; and

- Clarify that the obligations of an ERISA fiduciary in respect of supervision of an investment manager of a pooled investment vehicle would be limited to confirming that the investment manager has voted in accordance with such policies.

We discuss each of these recommendations in more detail below.

Discussion

We agree with the general principles articulated in the Proposed Rule regarding the application of the fiduciary duty under ERISA to the management of shareholder rights appurtenant to shares of stock, including the right to vote proxies. In particular, we agree that when deciding whether and how to exercise those rights fiduciaries must carry out their duties prudently and solely in the interests of the participants and beneficiaries and for the exclusive purposes of: (i) providing benefits to participants and beneficiaries; and (ii) defraying the reasonable expenses of administering the plan pursuant to ERISA sections 403 and 404.[3]

The Proposed Rule includes an enumerated list of six obligations (the "Enumerated Obligations") with which a fiduciary must comply in order to fulfill its fiduciary duty in proxy voting and exercising other shareholder rights, including: (i) acting solely in accordance with the economic interests of plan participants and beneficiaries; (ii) considering the likely impact on the investment performance, taking into account the size of the position and the costs involved; (iii) not subordinating the interests of the participants and beneficiaries to any non-pecuniary objective; (iv) investigating material facts that form the basis for any particular proxy vote or other exercise of shareholder rights, including specific requirements when adopting a proxy adviser's voting guidelines; (v) maintaining records that demonstrate the basis for particular proxy votes and exercises of shareholder rights; and (vi) exercising prudence and diligence in the selection and monitoring of any proxy advisers or other service providers.[4]

The Proposed Rule then provides that a plan fiduciary *must* vote any proxy where the fiduciary prudently determines that the matter being voted upon would have an economic impact on the plan after considering the Enumerated Obligations and taking into account the costs involved (including the cost of research, if necessary, to determine how to vote), and *must not* vote unless the fiduciary prudently determines that the matter being voted upon would have an economic impact on the plan based on the same considerations.[5] In discussing these requirements, the Release states, "[i]n the [DOL]'s view, fiduciaries must be prepared to articulate the anticipated economic benefit of proxy-vote decisions in the event they decide to vote.[6]

Recognizing that the costs involved in determining whether a vote is required or prohibited under this standard may be resource-intensive and outweigh any potential benefits to the plan in actually exercising proxy voting rights, the Proposed Rule includes potential options ("Permitted Practices") for fiduciaries that are intended to reduce the need for fiduciaries to consider proxy votes

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3 *See* Proposed Rule paragraphs (e)(1) and (2)(i).

4 Proposed Rule paragraph (e)(2)(ii).

5 Proposed Rule paragraphs (e)(3)(i) and (ii).

6 Release at 55,224.

that are unlikely to have an economic impact on the plan, thereby allowing plans to focus resources on matters most likely to have an economic impact.[7] Specifically, the Proposed Rule allows plans to adopt proxy voting policies that include specific parameters reasonably designed to serve the plan's economic interest.[8]

We agree with the DOL that it is important for ERISA fiduciaries to able to rely on reasonably designed proxy voting policies consistent with the Permitted Practices to meet their fiduciary obligations. In order to ensure that ERISA fiduciaries can realize the benefits of the proposed Permitted Practices, we encourage the DOL to provide further clarifications regarding their application in practice, as discussed in more detail below.

1. DOL Should Clarify the Interaction of the Permitted Practices with the Enumerated Obligations in Order to Avoid Imposing Undue Costs and Burdens on ERISA Fiduciaries and Third-Party Investment Managers

In our view, the effective operation of the Proposed Rule's Permitted Practices is critical to achieving the DOL's overarching goals in issuing the proposal, namely, for ERISA fiduciaries to focus on activities most likely to have an economic impact on a plan's investment and ensure that plan fiduciaries only incur costs to vote proxies and exercise other shareholder rights that the fiduciary reasonably determines are economically justified. Indeed, in light of the structure of the Proposed Rule and certain statements in the Release—where either voting or not voting proxies may be an express violation of the Proposed Rule, and even expending resources to determine whether voting is or is not required under the Proposed Rule may itself be a violation—proxy voting policies consistent with the Permitted Practices are likely to be widely, if not universally, adopted.[9]

We believe that the Permitted Practices, as proposed, go a long way in furthering the DOL's stated goals in issuing the Proposed Rule. Importantly, the rule text is clear that the Permitted Practices listed in the Proposed Rule are "example[s]" and therefore neither exclusive nor exhaustive. The Release also includes helpful guidance, which we suggest the DOL reaffirm in the adopting release, indicating that a fiduciary has the flexibility to adopt proxy voting policies that encompass any one or more of the Permitted Practices (including alternative practices, as appropriate), allowing for a wide range of prudently adopted proxy voting policies. Without certain clarifications, however, we believe the Proposed Rule may result in some uncertainty and, in light of the potential liability that ERISA fiduciaries could face, undermine the full benefits that the Proposed Rule would provide through the Permitted Practices. Accordingly, we suggest several important clarifications.

First, the DOL should clarify that an ERISA fiduciary will be deemed to satisfy the Enumerated Obligations if the fiduciary votes in accordance with prudently adopted proxy voting

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7 *See* Release at 55,225.

8 The Proposed Rule includes several examples of these Permitted Practices, including voting in accordance with management recommendations on routine matters, focusing on certain matters likely to have a significant impact on the value of the plan's investments (e.g., mergers and other corporate events) and refraining from voting for investments below a certain quantitative threshold. Proposed Rule paragraphs (e)(3)(iii)(A)-(C).

9 For example, the Release states that "the expenditure of plan resources to decide whether and how to vote on other proposals that are unlikely to have an impact on a plan's economic value may be unwarranted and, given the particular facts and circumstances, could constitute a fiduciary breach." Release at 55,232.

policies that are consistent with the Permitted Practices. Although the Release in several instances suggests this result, as currently structured, it is not entirely clear whether and to what extent any of the Enumerated Obligations would require further action when an ERISA fiduciary or an investment manager that has been delegated proxy voting authority votes in accordance with proxy voting policies consistent with the Permitted Practices. For example, the Enumerated Obligations require that an ERISA fiduciary maintain "records on proxy voting activities and other exercises of shareholder rights, including records that demonstrate *the basis for particular proxy votes* and exercises of shareholder rights."[10] The final rule should be clear that as long as proxy voting policies are prudently adopted and reviewed at least once every two years in accordance with paragraphs (e)(3)(iii) and (iv) of the Proposed Rule, no additional documentation demonstrating the basis for particular proxy votes will be required.[11] Similarly, the Enumerated Obligations to investigate material facts that form the basis for any particular proxy vote[12] and to exercise oversight of proxy advisory firms and other service providers[13] should be limited to confirming that proxies are voted in accordance with such proxy voting policies.

Second, the DOL should specifically provide in the rule text that ERISA fiduciaries will not be subject to liability for engaging in (or abstaining from) voting proxies in accordance with prudently adopted policies that are consistent with the Permitted Practices. While we believe this to be the intent of the Proposed Rule, the rule text expressly provides exculpation from liability only in the circumstances where an ERISA fiduciary prudently *deviates from* the adopted proxy voting policies.[14] Providing a clear path for compliance with regard to proxy voting will reduce costs that may be borne by plan participants and beneficiaries.

In addition, the DOL should clarify that although the Proposed Rule *permits* an ERISA fiduciary to prudently deviate from its proxy voting policies, it does not create an affirmative obligation on the ERISA fiduciary to determine whether it would be prudent to deviate from its proxy voting policies with regard to any particular vote. Such an obligation would significantly undermine the utility of the Permitted Practices which, as noted above, were expressly designed to ensure that ERISA fiduciaries are not required to expend resources to determine whether a particular vote is required or prohibited, as the cost of doing so could outweigh any potential benefits to the plan in actually voting.

Finally, in order to avoid imposing duplicative and unnecessary costs, the Release should provide more clarity that an SEC-registered investment adviser that has complied with its fiduciary duty under the Investment Advisers Act of 1940 with regard to proxy voting, as illustrated in the SEC's 2019 Proxy Voting Guidance, will satisfy the obligations under the Proposed Rule with respect to proxy voting, as long as its proxy voting policies are consistent with the Permitted Practices. While the Release endorses the SEC's 2019 Proxy Voting Guidance in a number of

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[10] Proposed Rule paragraph (e)(3)(ii)(E) (emphasis added).

[11] In response to the DOL's specific request for comment, we support the proposed requirement that proxy voting policies adopted pursuant to paragraph (e)(3)(iv) must be reviewed every two years. We believe more frequent review would impose costs on ERISA fiduciaries and third-party investment managers that are not justified by any potential benefits.

[12] Proposed Rule paragraph (e)(3)(ii)(D).

[13] Proposed Rule paragraph (e)(3)(ii)(F).

[14] Proposed Rule paragraph (e)(3)(v).

respects, including with regard to the types of proxy voting policies that may be consistent with the Permitted Practices, the Release suggests that additional actions may be required under ERISA (e.g., with respect to retaining and monitoring a proxy advisory firm).[15] If compliance with SEC rules and guidance is insufficient for this purpose, the DOL should more clearly specify what additional actions are required and also seek to ensure that any additional actions are consistent with the SEC rules, to avoid potentially incompatible standards for ERISA fiduciaries and SEC-registered investment managers. This clarity and consistency will help avoid unnecessary costs and burdens in administering plan assets which would be contrary to the purposes of the Proposed Rule.

2. <u>DOL Should Expressly Clarify that Third-Party Investment Managers Will Comply with the Proposed Rule by Voting in Accordance with Proxy Voting Policies that Are Consistent with the Permitted Practices</u>

The Release recognizes that third-party asset managers will assume responsibility for proxy voting on behalf of plan investors in many cases.[16] The Release also recognizes that responsible fiduciaries might increase their demand for asset managers to implement separate policies customized for particular ERISA plans or for ERISA plans generally that align with the Permitted Practices.[17]

However, in addition to the provisions of the Proposed Rule that generally apply to ERISA fiduciaries, the Proposed Rule includes requirements that are applicable to investment managers that have been delegated the authority to vote proxies or exercise shareholder rights. First, the Proposed Rule provides that a responsible plan fiduciary must require such an investment manager:

> 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.[18]

As recognized throughout the Release, the costs associated with determining the economic benefits of any particular proxy vote on an individual basis may in many cases not be justified economically. The Release also implies that documenting the basis for any particular proxy vote would be required of an investment manager *only* when the vote goes against the investment

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15 *See* Release at 55,224-5, n. 56 ("In the event fiduciaries believe the retention of a proxy advisory firm is appropriate, the [DOL] likewise views the SEC's guidance as reasonable direction for the diligence that ERISA plan fiduciaries should perform when reviewing and assessing a proxy advisory firm. The [DOL] notes, however, that the SEC standards do not necessarily capture all the actions that ERISA may require as a result of that review and assessment.").

16 *See* Release at 55,232 ("The [DOL] understands that under the proposal, most of the relevant fiduciary duties will reside with, and most of the required activities will be performed by, third-party asset managers, as is already common practice. Such asset managers are often large and provide the relevant fiduciary services for a large number of plans.").

17 Release at 55,235.

18 Proposed Rule paragraph (e)(2)(iii).

manager's internal policy (and even then, the documentation would be quite limited).[19] However, neither the text of the Proposed Rule nor the guidance in the Release expressly states that the above requirement can be met where an investment manager votes in accordance with prudently adopted proxy voting policies that are consistent with the Permitted Practices.

Consistent with our recommendation in Section 1, we suggest that the DOL clarify that an investment manager would satisfy the above requirement by voting in accordance with prudently adopted proxy voting policies that are consistent with the Permitted Practices. As recognized in the Release, SEC-registered investment advisers are required, as part of their ongoing SEC compliance program, to review and document at least annually the adequacy of their voting policies to ensure that they have been formulated reasonably and implemented effectively, including that they continue to be reasonably designed to ensure that the adviser casts votes on behalf of its clients in the best interest of such clients.[20] To the extent the DOL believes that proxy advisory firms or other service providers should be subject to heightened documentation requirements, we suggest that this provision of the Proposed Rule be revised to remove investment managers that have been delegated proxy voting authority from the scope of such requirements.

Second, with respect to investment managers of a pooled investment vehicle that holds assets of more than one employee benefit plan, the Proposed Rule expressly permits the investment manager to develop an investment policy statement consistent with Title I of ERISA and the Proposed Rule, and require participating plans to accept the investment manager's investment policy, including any proxy voting policy, before they are allowed to invest.[21] 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 the Proposed Rule before deciding to retain the investment manager.

We support this aspect of the Proposed Rule. However, the Release provides virtually no guidance on this provision or any discussion on how the other provisions of the Proposed Rule would interact with it.[22] We believe this could lead to uncertainty both for ERISA plan fiduciaries that invest in pooled investment vehicles, and for the investment managers of those pooled investment vehicles, with regard to their compliance obligations under the Proposed Rule. Consistent with our recommendations above, we believe that the adopting release for the final rule should specifically state that an ERISA fiduciary investing in a pooled investment vehicle and the investment manager of the pooled investment vehicle will be deemed to satisfy the Enumerated Obligations of the Proposed Rule so long as the investment manager votes in accordance with

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19 *See* Release at 55,225 ("When an investment manager's rationale on a vote for recurring issues is to follow a uniform internal policy, the manager should document the reasons for any vote that goes against the policy, which would generally only require a brief explanation directly in the proxy-voting record.").

20 *See* 2019 SEC Proxy Voting Guidance at 47,424; Release at 55,223.

21 Proposed Rule paragraph (e)(4)(ii). Absent the adoption of such an investment policy, ERISA section 404(a)(1)(D) requires the investment manager to reconcile, insofar as possible, any conflicting policies of more than one employee benefit plan. 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.

22 We recognize that this provision is largely carried over from Interpretive Bulletin 2016-01, which is stated in the Release as no longer representing the view of the DOL regarding the proper interpretation of ERISA with respect to the exercise of shareholder rights by fiduciaries of ERISA-covered plans.

prudently adopted proxy voting policies that are consistent with the Permitted Practices, and that the obligations of the ERISA fiduciary and the investment manager in respect of supervision and documentation, respectively, would be limited to confirming that the investment manager has voted (or abstained from voting) in accordance with such policies.

MFA[23] and AIMA[24] appreciate the opportunity to contribute to the DOL's efforts to set forth a regulatory structure to assist ERISA fiduciaries in navigating ESG investment trends. If you have any questions about these comments, please do not hesitate to contact the undersigned at (ballensworth@managedfunds.org) or (ajacobs-dean@aima.org).

Respectfully submitted,

/s/ Benjamin Allensworth

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Managing Director, Head of Markets,
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[23] The Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry's contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and many other regions where MFA members are market participants.

[24] The Alternative Investment Management Association (AIMA) is the global representative of the alternative investment industry, with around 2,000 corporate members in over 60 countries. AIMA's fund manager members collectively manage more than $2 trillion in hedge fund and private credit assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programs and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. AIMA set up the Alternative Credit Council ("ACC") to help firms focused in the private credit and direct lending space. The ACC currently represents over 170 members that manage $400 billion of private credit assets globally. AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation ("CAIA"), the first and only specialized educational standard for alternative investment specialists. AIMA is governed by its Council Directors).