DEPARTMENT OF LABOR

Employee Benefits Security Administration

29 CFR Parts 2509 and 2550

RIN 1210–AB91

Fiduciary Duties Regarding Proxy Voting and Shareholder Rights

AGENCY: Employee Benefits Security Administration, Department of Labor.

ACTION: Final rule.

SUMMARY: The Department of Labor (Department) is amending the ''Investment Duties'' regulation to address the application of the prudence and exclusive purpose duties under the Employee Retirement Income Security Act of 1974 (ERISA) to the exercise of shareholder rights, including proxy voting, the use of written proxy voting policies and guidelines, and the selection and monitoring of proxy advisory firms. This document also removes Interpretive Bulletin 2016–01 from the Code of Federal Regulations as it no longer represents the view of the Department regarding the proper interpretation of ERISA with respect to the exercise of shareholder rights by fiduciaries of ERISA-covered plans.

DATES: *Effective Date:* The final rule is effective on January 15, 2021.

Applicability Dates: See Section B.3(vi) of this document and § 2550.404a–1(g) of the final rule for compliance dates for § 2550.404a–1(e)(2)(ii)(D) and (E), (e)(2)(iv), (e)(4)(ii) of the final rule.

FOR FURTHER INFORMATION CONTACT: Jason A. DeWitt, Office of Regulations and Interpretations, Employee Benefits Security Administration, (202) 693–8500. This is not a toll-free number.

Customer Service Information: Individuals interested in obtaining information from the Department of Labor concerning ERISA and employee benefit plans may call the Employee Benefits Security Administration (EBSA) Toll-Free Hotline, at 1–866–444–EBSA (3272) or visit the Department of Labor's website (*www.dol.gov/agencies/ebsa*).

SUPPLEMENTARY INFORMATION:

A. Background and Purpose of Regulatory Action

Title I of the Employee Retirement Income Security Act of 1974 (ERISA) establishes minimum standards for the operation of private-sector employee benefit plans and includes fiduciary responsibility rules governing the conduct of plan fiduciaries.[1] In connection with proxy voting, the Department's longstanding position is that the fiduciary act of managing plan assets includes the management of voting rights (as well as other shareholder rights) appurtenant to shares of stock. In carrying out these duties, ERISA mandates that fiduciaries act ''prudently'' and ''solely in the interest'' and ''for the exclusive purpose'' of providing benefits to participants and their beneficiaries.[2]

This regulatory project was undertaken, in part, to confirm that, when exercising shareholder rights, ERISA plan fiduciaries may not subordinate the interests of plan participants and beneficiaries in receiving financial benefits under a plan to non-pecuniary objectives.[3] This duty of loyalty—a bedrock principle of ERISA, with deep roots in the common law of trusts—requires those serving as fiduciaries to act with a single-minded focus on the interests of beneficiaries. The duty of prudence prevents a fiduciary from choosing an investment alternative that is financially less beneficial than reasonably available alternatives. The Supreme Court has described the duty of loyalty as requiring that fiduciaries act with an ''eye single'' to the interests of participants and beneficiaries,[4] and appellate courts have described ERISA's fiduciary duties as ''the highest known to the law.'' [5] The subject of this rulemaking is how these ERISA fiduciary duties apply to the exercise of shareholder rights by ERISA-covered plans, as a result of the Department's belief that confusion exists among some fiduciaries and other stakeholders with respect to the exercise of shareholder rights, perhaps due in part to varied statements the Department has made on the consideration of non-pecuniary or non-financial factors over the years in sub-regulatory guidance on these activities.

The Department began interpreting the duties of prudence and loyalty and issuing sub-regulatory guidance in the area of proxy voting and the exercise of shareholder rights in the 1980s. The Department issued an opinion letter to Avon Products, Inc. in 1988 (the Avon Letter), in which the Department took the position that, while the fiduciary act of managing plan assets that are shares of corporate stock includes the voting of proxies appurtenant to those shares, the named fiduciary of a plan has a duty to monitor decisions made and actions taken by investment managers with regard to proxy voting.[6]

Subsequent to the Avon Letter, the Department issued additional guidance concerning fiduciary duties in the context of exercising shareholder rights. In 1994, the Department issued its first interpretive bulletin on proxy voting, Interpretive Bulletin 94–2 (IB 94–2).[7] IB 94–2 recognized that fiduciaries may engage in shareholder activities intended to monitor or influence corporate management in situations where the responsible fiduciary concludes that, after taking into account the costs involved, there is a reasonable expectation that such shareholder activities (by the plan alone or together with other shareholders) will enhance the value of the plan's investment in the corporation. The Department expected that increased shareholder engagement by pension funds—encouraged by the new interpretive bulletin—would improve corporate performance and help ensure companies treated their employees well.[8] However, the Department also reiterated its view that ERISA does not permit fiduciaries, in voting proxies or exercising other shareholder rights, to subordinate the

[1] Throughout this preamble, the Department's discussion of plan fiduciaries includes named fiduciaries under the plan, along with any persons that named fiduciaries have designated to carry out fiduciary responsibilities as permitted under ERISA section 405(c)(1). Similarly, references to proxy voting also encompass situations in which a fiduciary directly casts a vote in a matter (*e.g.,* voting in person at a shareholder meeting) rather than by proxy.

[2] ERISA section 404(a)(1). *See also* ERISA section 403(c)(1) (''[T]he assets of a plan shall never inure to the benefit of any employer and shall be held for the exclusive purposes of providing benefits to participants in the plan and their beneficiaries'').

[3] *Fifth Third Bancorp* v. *Dudenhoeffer,* 573 U.S. 409, 421 (2014) (the ''benefits'' to be pursued by ERISA fiduciaries as their ''exclusive purpose'' does not include ''nonpecuniary benefits'') (emphasis in original).

[4] *Pegram* v. *Herdrich,* 530 U.S. 211, 235 (2000) (quoting *Donovan* v. *Bierwirth,* 680 F.2d 263, 271 (2d Cir. 1982)).

[5] *See, e.g., Tibble* v. *Edison Int'l,* 843 F.3d 1187, 1197 (9th Cir. 2016).

[6] Letter to Helmuth Fandl, Chairman of the Retirement Board, Avon Products, Inc. 1988 WL 897696 (Feb. 23, 1988). Only a few commenters on the proposal mentioned the Avon Letter, either supporting the views taken in the letter as being consistent with other professional codes of ethics or asserting that the proposed rule reversed the intent of the Avon Letter by establishing a presumption that voting proxies is a cost to be minimized and not an asset to be prudently managed.

[7] 59 FR 38860 (July 29, 1994).

[8] *See* 1994 DOL Press Conference, at 2–4, 10, 15–16; *see also* Leslie Wayne, *U.S. Prodding Companies to Activism on Portfolios,* N.Y. Times (July 29, 1994), *www.nytimes.com/1994/07/29/business/us-prodding-companies-to-activism-on-portfolios.html* (quoting official stating that the Department is ''trying to encourage corporations to be activist owners,'' and that ''such activism is consistent with your fiduciary duty and we expect it will improve your corporate performance'').

economic interests of participants and beneficiaries to unrelated objectives.

In October 2008, the Department replaced IB 94–2 with Interpretive Bulletin 2008–02 (IB 2008–02).[9] The Department's intent was to update the guidance in IB 94–2 and to reflect interpretive positions issued by the Department after 1994 on shareholder engagement and socially-directed proxy voting initiatives. IB 2008–02 stated that fiduciaries' responsibility for managing proxies includes both deciding to vote or not to vote.[10] IB 2008–02 further stated that the fiduciary duties described at ERISA sections 404(a)(1)(A) and (B) require that in voting proxies the responsible fiduciary shall consider only those factors that relate to the economic value of the plan's investment and shall not subordinate the interests of the participants and beneficiaries in their retirement income to unrelated objectives. In addition, IB 2008–02 stated that votes shall only be cast in accordance with a plan's economic interests. IB 2008–02 explained that if the responsible fiduciary reasonably determines that the cost of voting (including the cost of research, if necessary, to determine how to vote) is likely to exceed the expected economic benefits of voting, the fiduciary has an obligation to refrain from voting.[11] The Department also reiterated in IB 2008–02 that any use of plan assets by a plan fiduciary to further political or social causes ''that have no connection to enhancing the economic value of the plan's investment'' through proxy voting or shareholder activism is a violation of ERISA's exclusive purpose and prudence requirements.[12]

In 2016, the Department issued Interpretive Bulletin 2016–01 (IB 2016–01), which reinstated the language of IB 94–2 with certain modifications.[13] IB 2016–01 reiterated and confirmed that ''in voting proxies, the responsible fiduciary [must] consider those factors that may affect the value of the plan's investment and not subordinate the interests of the participants and beneficiaries in their retirement income to unrelated objectives.'' [14] In further interpreting ERISA's duties, the Department has stated that it has rejected a construction of ERISA that would render the statute's tight limits on the use of plan assets illusory and that would permit plan fiduciaries to expend trust assets to promote myriad public policy preferences, including through shareholder engagement activities, voting proxies, or other investment policies.[15]

On September 4, 2020, the Department published in the **Federal Register** a proposed rule to amend the ''Investment Duties'' regulation at 29 CFR 2550.404a-1 (Investment Duties regulation) to address the prudence and loyalty duties under sections 404(a)(1)(A) and 404(a)(1)(B) of ERISA in the context of proxy voting and other exercises of shareholder rights by the responsible ERISA plan fiduciaries, the use of written proxy voting policies and guidelines, and the selection and monitoring of proxy advisory firms.[16] The Department explained its belief that addressing the application of ERISA fiduciary obligations with respect to exercise of shareholder rights, including proxy voting, through notice-and-comment regulatory action under the Administrative Procedure Act was appropriate and would benefit ERISA plan fiduciaries and plan participants.

This regulatory project also was initiated to respond to a number of other issues. The Department was concerned, for example, that the Avon Letter and subsequent sub-regulatory guidance from the Department has resulted in a misplaced belief among some stakeholders that fiduciaries must always and in every case vote proxies, subject to limited exceptions, in order to fulfill their obligations under ERISA.[17] Further, the Department was responding to significant changes in the way ERISA plans invest and changes in the investment world more broadly since the Department first issued guidance on these topics in 1988. Widespread shareholder activism and corporate takeovers at that time created an intense focus on shareholder voting by ERISA plans and confusion as to how fiduciary standards applied to such voting.

The Department described in the proposal a variety of changes in proxy voting policies and behavior, including an increase in the percentage of individual securities held by, and plan assets managed by, institutional investors, diminishing the scope of proxy voting rights and obligations attributable to individual securities held by ERISA plans.[18] At the same time, since the 1980s, the type of investments held by ERISA plans has changed, for example through the development and growth of exchange-traded funds, sector-based equity products, hedge funds, and passive investments. The proportion of ERISA plan assets held in alternative investments like hedge, private equity, and venture capital funds has grown significantly.[19] When issuing the proposed rule, the Department cited evidence that investors continue to add to the set of factors considered in their review and analysis of corporate practices.[20]

The Department also took note of the issues and concerns identified during the U.S. Securities and Exchange Commission's (SEC's) ongoing proxy reform initiative.[21] Pursuant to the 2019

[9] 73 FR 61731 (Oct. 17, 2008).

[10] Id. at 61732.

[11] Id.

[12] Id. at 61734.

[13] 81 FR 95879 (Dec. 29, 2016). In addition, the Department issued a Field Assistance Bulletin to provide guidance on IB 2016–01 on April 23, 2018. *See* FAB 2018–01, at *www.dol.gov/sites/dolgov/files/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2018-01.pdf.*

[14] Id. at 95882.

[15] *See* id. at 95881.

[16] 85 FR 55219 (Sept. 4, 2020).

[17] *See, e.g.,* Barbara Novick, *Revised and Extended Remarks at Harvard Roundtable on Corporate Governance Keynote Address ''The Goldilocks Dilemma''* (Nov. 6, 2019), *www.blackrock.com/corporate/literature/publication/barbara-novick-remarks-harvard-roundtable-corporate-governance-the-goldilocks-dilemma-110619.pdf,* at 15 (Avon Letter indicated ''that asset managers should generally vote shares as part of their fiduciary duty''); *see* Former SEC Commissioner 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); Manifest Information Services Ltd, *Response to ESMA Discussion Paper 'An Overview of the Proxy Advisory Industry: Considerations on Possible Policy Options'* (June 2012), *www.osc.gov.on.ca/documents/en/Securities-Category2-Comments/com_20120622_25–401_wilsons.pdf,* at 37 (comment letter from European proxy voting agency describing DOL proxy guidance as concerning ''duties of . . . fiduciaries . . . to vote the shares in companies held by their pension plans''); Charles M. Nathan, *The Future of Institutional Share Voting: Three Paradigms* (July 23, 2010), *https://corpgov.law.harvard.edu/2010/07/23/the-future-of-institutional-share-voting-three-paradigms/* (''the current system for voting portfolio securities by application of uniform voting policies . . . is perceived as successfully addressing the commonly understood fiduciary duty of institutional investors to vote all of their portfolio securities on all matters''). *See also* U.S. Department of Labor, Transcript of Press Conference on Corporate Activist Role in Pension Planning (July 28, 1994), at 15–16 (then-Secretary Robert Reich stating that IB 94–2 ''makes very clear that . . . pension fund managers, trustees, [and] fiduciaries have an obligation to vote proxies'' unless the costs ''substantially outweigh'' the benefits) (1994 DOL Press Conference).

[18] 85 FR 55219 at 55221–22 (Sept. 4, 2020).

[19] *See id.,* at 55222.

[20] Kosmas Papadopoulos, *The Long View: US Proxy Voting Trends on E&S Issues from 2000 to 2018,* Harvard Law School Forum on Corporate Governance (Jan. 31, 2019), *https://corpgov.law.harvard.edu/2019/01/31/the-long-view-us-proxy-voting-trends-on-es-issues-from-2000-to-2018,* (2019 ISS Proxy Voting Trends).

[21] *See, e.g.,* Commission Guidance Regarding Proxy Voting Responsibilities of Investment

Continued

SEC Guidance, where an investment adviser has the authority to vote on behalf of its client, the investment adviser, among other things, must have a reasonable understanding of the client's objectives and must make voting determinations that are in the best interest of the client. Under this guidance, for an investment adviser to form a reasonable belief that its voting determinations are in the best interest of the client, the investment adviser should conduct an investigation reasonably designed to ensure that the voting determination is not based on materially inaccurate or incomplete information. The 2019 SEC Guidance also provides that investment advisers that retain proxy advisory firms to provide voting recommendations or voting execution services should consider additional steps to evaluate whether the voting determinations are consistent with the investment adviser's voting policies and procedures, and in the client's best interest before the votes are cast. The 2019 SEC Guidance provides that investment advisers should consider whether the proxy advisory firm has the capacity and competency to adequately analyze the matters for which the investment adviser is responsible for voting. The 2019 SEC Guidance also explains that an investment adviser's decision regarding whether to retain a proxy advisory firm should also include a reasonable review of the proxy advisory firm's policies and procedures regarding how it identifies and addresses conflicts of interest. Further, as part of the investment adviser's ongoing compliance program, the investment adviser must, no less frequently than annually, review and document the adequacy of its voting policies and procedures.

The SEC also adopted regulatory amendments that, among other things, require proxy advisory firms that are engaged in a solicitation to provide specified disclosures, adopt written policies and procedures reasonably designed to ensure that proxy voting advice is made available to securities issuers, and provide proxy advisory firm clients with a mechanism by which the clients can reasonably be expected to become aware of a securities issuer's views about the proxy voting advice, so that the clients can take such views into account as they vote proxies.[22] The SEC issued supplemental guidance to assist investment advisers in assessing how to consider the additional information that may become more readily available to them as a result of these amendments, including in circumstances when the investment adviser uses a proxy advisory firm's electronic vote management system that ''pre-populates'' the adviser's proxies with suggested voting recommendations and/or for voting execution services.[23]

The proposal on proxy voting and shareholder rights provided the Department with a vehicle to coordinate many of the fiduciary concepts concerning investing according to the pecuniary interests of plans with the rules governing the use of plan resources on proxy voting and the exercise of other shareholder rights.[24] A more detailed discussion of the basis for the rulemaking and the evidence supporting the proposal can be found in the preamble to the Department's proposal.[25] As discussed throughout this preamble, the final rule reflects significant modifications to the proposal based on the public record and commenters' feedback. The Department continues to believe that enhancing the effectiveness and efficiency of the proxy voting process for ERISA plans is an important goal. This process will be improved to the extent ERISA plan fiduciaries better understand how to make informed decisions when executing shareholder rights in compliance with ERISA's obligations of prudence and loyalty—specifically that the execution of such rights must be conducted in a manner to ensure that plan resources are not inappropriately allocated. The Department also believes that this rule is necessary to modernize standards for ERISA plan fiduciaries in this context, for example to recognize that proxy voting advice businesses, such as proxy advisory firms, now play a more significant role in the proxy voting process. It is not the Department's intention to judge the value of any specific proposal to be voted upon, for example, or to take a position on the merits of any particular topic. Rather, the Department intends only to address the standards according to which plan fiduciaries must make such judgments, a goal that the Department believes is more appropriately advanced in light of revisions made in the final rule.

The Department invited interested persons to submit comments on the proposed rule, and in response received approximately 300 written comments from a variety of parties, including plan sponsors and fiduciaries, plan service and investment providers (including investment managers and proxy voting firms), and employee benefit plan and participant representatives. The Department also received approximately 6,700 submissions in response to petitions. The comments are available for review on the ''Public Comments'' page under the ''Laws and Regulations'' tab of the Department's Employee Benefits Security Administration website.[26]

B. Final Rule

After evaluating the full range of public comments and extensive record developed on the proposal, the final rule as described below amends the Investment Duties regulation to address the prudence and loyalty duties under sections 404(a)(1)(A) and 404(a)(1)(B) of ERISA in the context of proxy voting and other exercises of shareholder rights by responsible ERISA plan fiduciaries. The Department anticipates that actions taken by the SEC as part of its proxy reform initiative may result in changes in practices among investment advisers and proxy advisory firms that will help address some of the Department's concerns about ERISA fiduciaries properly discharging their duties with respect to proxy voting activities and appropriately selecting and overseeing proxy advisory firms. However, the Department continues to believe that notice-and-comment rulemaking in this area is appropriate, in part because the Department's existing sub-regulatory guidance may have created a perception that ERISA fiduciaries must vote proxies on every proposal. In the Department's view, a regulation in this area will address the misunderstanding that exists on the part of some stakeholders that ERISA fiduciaries are required to vote all proxies and, to the extent that proxies are voted, direct fiduciaries to act in a manner consistent with the economic interests of plans and plan participants that does not subordinate their interests to any non-pecuniary objectives or promote goals unrelated to the financial interests of participants and beneficiaries.

Some commenters complained that the 30-day comment period was too short given the complexity of issues involved, the magnitude of such changes to the current marketplace

Advisers, 84 FR 47420 (Sept. 10, 2019) (2019 SEC Guidance).

[22] *See* Exemptions from the Proxy Rules for Proxy Voting Advice, 85 FR 55082 (Sept. 3, 2020) (2020 SEC Proxy Voting Advice Amendments).

[23] *See* Supplement to Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, 85 FR 55155 (Sept. 3, 2020) (2020 SEC Supplemental Guidance).

[24] 85 FR at 55219.

[25] *Id.*, beginning at 55221 and in the proposed regulatory impact analysis beginning at 55227.

[26] *See www.dol.gov/agencies/ebsa/laws-and-regulations/rules-and-regulations/public-comments.*

practices related to proxy voting and other exercises of shareholder rights, and the need to prepare supporting data. Many commenters requested an extension of the comment period and that the Department schedule a public hearing on the proposal and allow the public record to remain open for post-hearing comments from interested parties. The Department has considered these requests, but has determined that it is neither necessary nor appropriate to extend the public comment period, hold a public hearing, or withdraw or republish the proposed regulation. A substantial and comprehensive public comment record was developed on the proposal sufficient to substantiate promulgating a final rule. The scope and depth of the public record that has been developed itself belies arguments that a 30-day comment period was insufficient. In addition, most issues relevant to the proposal have been analyzed and reviewed by the Department and the public in the context of three separate Interpretive Bulletins issued in 1994, 2008, and 2016 and the public feedback that resulted. Finally, public hearings are not required under the Department's general rulemaking authority under section 505 of ERISA, nor under the Administrative Procedure Act's procedures for rulemaking at 5 U.S.C. 553(c). In this case, a public hearing is not necessary to supplement an already comprehensive public record.

Thus, this final rulemaking follows the notice-and-comment process required by the Administrative Procedure Act, and fulfills the Department's mission to protect, educate, and empower retirement investors. This rule is considered to be an Executive Order (E.O.) 13771 regulatory action. Details on the estimated costs of this rule can be found in the final rule's economic analysis. The Department has concluded that the additions to the Investment Duties regulation and the rule's improvements as compared to the Department's previous sub-regulatory guidance are appropriate and warranted. The final rule furthers the paramount goal of ERISA plans to provide a secure retirement for American workers. Accordingly, after consideration of the written comments received, the Department has determined to adopt the proposed regulation as modified and set forth below. As explained more fully below, the final regulation contains several important changes from the proposal in response to public comments.

1. General Public Comments and Adoption of a Principles-Based Approach

In response to the proposed rule, the Department received a considerable amount of support and opposition from interested parties.

Commenters supporting the rule argued that the proposed rule was essential because the Department's existing sub-regulatory guidance has created a perception that ERISA fiduciaries must vote proxies on every proposal. This rulemaking, according to some commenters, would provide certainty to plan fiduciaries and benefit ERISA plan participants, by ensuring that plan resources will be expended only on proxy research and voting matters that are necessary to protect the economic interests of plan participants. Commenters supporting the proposal endorsed the Department's view that these rights must be exercised with a singular focus in mind—the *economic* interests of ERISA plan participants and beneficiaries. They agreed that in a rapidly changing investment landscape, plan fiduciaries and asset managers should not be influenced by non-financial interests. For example, some commenters explained that it is the duty of ERISA fiduciaries to reject attempts to advance political or social objectives at the expense of investment returns, growth, and stability for individuals saving for retirement, the very population that the Department, through ERISA, has been charged to protect. As one commenter explained, ERISA fiduciary duties are predicated on trust law, and trusts must be managed to the advantage of formally named beneficiaries—in this case plan participants and their beneficiaries—and not to benefit corporate management or vague notions of societal good as determined by other parties. Some commenters argued that proxy advisory firms, which often assist with proxy voting, have an outsized influence on voting decisions and have ''taken sides'' politically and socially.

A number of commenters agreed in general with the Department's position on these issues, and some provided additional information substantiating the need for, and propriety of, the Department's proposed approach to managing proxy voting practices. Some further argued that, although exercising shareholder rights on the basis of environmental, social, or governance factors (commonly referred to as ''ESG'') may be welcomed by some private investors, proxy rights should be exercised only for financial matters that will help secure the retirement of plan participants in the case of ERISA-covered pension and other retirement savings plans because when fiduciaries exercise proxy rights for non-financial reasons they are more likely to incur additional, unnecessary risks for investors that may not produce corresponding economic value. A few commenters supported the Department's assertion that the amount of ESG shareholder proposals has increased since 1988, as more such proposals are being put forward by groups with objectives other than increasing shareholder returns. While some commenters agreed with ESG proponents on the importance of environmental protections, social and political issues, and transparency in corporate governance, they nevertheless expressed their concern that proxy advisory firms, in particular, seem to have increasing power to promote these goals without the knowledge and agreement of a corporation's ''real'' owners, the shareholders, which include ERISA plans. They agreed that the Department has appropriately undertaken in this rulemaking to improve fiduciary oversight of these firms. Finally, commenters supporting the rule also said that any increased costs associated with the rule would be manageable, or, according to some commenters, that the rule would ultimately decrease plan costs and compliance burdens.[27]

Other commenters, however, objected to the Department's proposed rulemaking and raised a variety of legal and practical concerns. Some commenters who objected to the proposal requested that the Department withdraw the rule entirely, propose a different rule that takes a more principles-based approach to this subject matter, or wait until the Department analyzes the impact of its rule concerning ''Financial Factors in Selecting Plan Investments.'' [28] Alternatively, they argued that the Department should wait until the SEC establishes a track record of experience with its new proxy advisor and shareholder proposal rules, so that the Department can better align its guidance with the SEC's rules. Additionally, some commenters expressed the view that a principles-based approach would be consistent with the Investment Advisers Act of 1940 (Advisers Act) and the SEC's Rule 206(4)–6 thereunder and might help to reduce burdens for

[27] One commenter suggested that the rule may especially benefit fiduciaries of small plans, for whom the cost and burden of voting all proxies may be an impediment to sponsoring a plan.

[28] *See* 85 FR 72846 (Nov. 13, 2020).

fiduciaries in reconciling the Department's rule with the SEC's regulatory regime for investment advisers.

Some commenters opposing the proposed rule claimed that the Department failed to establish that there is in fact a problem with fiduciaries' exercise of shareholder rights and argued that the proposal, if finalized, would upset decades of Departmental precedent. These commenters further said that the approach taken in the proposal represented a burdensome and costly solution to a perceived problem without ''real life'' examples of any plans or participants and beneficiaries that have been harmed.

The Department does not believe that it is necessary to establish specific evidence of fiduciary misunderstandings or injury to plans or to plan participants in order to issue a regulation addressing the application of ERISA's fiduciary duties to the exercise of shareholder rights. Under the Department's authority to administer ERISA, the Department may promulgate rules that are preemptive in nature and is not required to wait for widespread harm to occur. The Department can thereby guard against injuries to plans and plan participants and beneficiaries and ensure prospective protections.

Regardless, there are several reasons for this rulemaking. First, the Department is aware that some plan fiduciaries and other parties have incorporated, or have considered incorporating, non-pecuniary factors into their proxy voting decisions. Further, as documented in the proposal, there is a history of statements from stakeholders and others evidencing misunderstanding of the Department's sub-regulatory guidance.[29] Finally, commenters on the proposal confirmed that fiduciaries may be over-relying on proxy advisory firms as a result of such confusion, by implementing advisory firms' voting recommendations without attention to whether the firms' policies are consistent with the economic interests of the plan. This final rule confirms that such decisions on proxy voting and other exercises of shareholder rights must be made pursuant to the duties of loyalty and prudence mandated by ERISA.

Some commenters argued that unless a number of clarifications and changes were made in the final rule, for example with respect to documentation and other requirements, the rule would be costly to implement and its standards costly to execute. Some commenters opposing the proposed rule argued that, not only is the rule unnecessary, but it would create new confusion for fiduciaries as they implement their duties under ERISA. According to these commenters, the rule would undermine fiduciaries' ability to act in what they believe to be the long-term economic interest of their plans' participants, which is a core statutory duty of fiduciaries to such participants. A few commenters provided an example of a potential ''trap'' that the proposal would create for fiduciaries, in that the rule would cause fiduciaries to not vote on a proposal for fear of violating the rule, but then later discover that they should in fact have voted on the proposal, effectively creating a breach of fiduciary duties. They claimed that the proposal was an example of ''government overreach'' that could dangerously impact the efficiency of the U.S. capital markets and the stability of the global economy.[30] The opposing commenters also argued that the proposal, if finalized, would disenfranchise ERISA plans, and thereby plan participants, as investors, by reducing the power and value of their shareholder rights, including the right to vote proxies.[31] Instead, voting power would be concentrated in the hands of non-ERISA investors, such as hedge funds, foreign investors, and other activist investors whose motivations may be based on short-term profits and non-economic factors, as well as in the hands of corporate management, as a result of the proposal's provision that, in these commenters' view, includes deference to management views.

Commenters opposing the proposed rule stated that, in voting on proposals, investors, including ERISA plans, generally decide matters that will hold management accountable and materially impact the long-term economic value of corporations. Some commenters argued that the proposal failed to recognize the potential long-term performance and economic impact of shareholder proposals on topics such as board independence and accountability—including opportunities to change a company's board of directors, diversity, approval of auditing firms, executive compensation policies—from either an individual investment or a wider portfolio perspective. These commenters disagreed with what they viewed as the Department's conclusion that ESG shareholder activity generally has little bearing on the value of corporate shares. Rather, these commenters claimed that a growing body of evidence demonstrates an increasing link between ESG activity, including the impact of ESG issues on a corporation's brand and reputation, and a corporation's long-term value. According to commenters, ESG factors may not appear to be economic on their face, yet all are fundamental corporate matters that often are critical to how companies strategize and manage risk, therefore impacting financial outcomes. As to proxy advisory firms, commenters opposing the rule argued that these firms engage in a rigorous process when making recommendations about proxy voting and that ongoing technological advances continue to enhance proxy voting transparency and effectiveness.

The final rule reflects a number of modifications made by the Department in response to the public comments. As in the proposal, the final rule amends the Investment Duties regulation in regard to proxy voting and the exercise of shareholder rights. The most significant adjustment from the proposal results from changes to make the final rule a more principles-based approach in response to commenters. The Department is persuaded that the complexity involved in a determination of economic versus non-economic impact would be costly to implement, and believes the core structure of the proposal that focused on whether a

[29] 85 FR 55219, 55230 (Sept. 4, 2020).

[30] A number of commenters asserted that the proposal was a not-so-thinly-veiled, policy-based judgment against the value of ESG shareholder proposals. They argued that this judgment is not the Department's to make; rather, it is the role of plan fiduciaries to make such judgments, and ESG proposals are material to shareholder decision-making and an important part of the due diligence of fiduciaries in constructing long-term, diversified portfolios. The Department disagrees with these commenters. This rulemaking project, similar to the recently published final rule on ERISA fiduciaries' consideration of financial factors in investment decisions, recognizes, rather than ignores, the economic literature and fiduciary investment experience that show a particular ''E,'' ''S,'' or ''G'' consideration may present issues of material business risk or opportunities to a specific company that its officers and directors need to manage as part of the company's business plan and that qualified investment professionals would treat as economic considerations under generally accepted investment theories. However, the Department recognizes that other ''E,'' ''S,'' or ''G'' factors may be non-pecuniary and a fiduciary should not assume that combining ESG factors into a single rating, index, or score creates an amalgamated factor that is itself pecuniary. Rather, this final rule and the financial factors rule sought to make clear that, from a fiduciary perspective, the relevant question is not whether a factor under consideration is ''ESG,'' but whether it is a pecuniary factor relevant to the exercise of a shareholder right or to an evaluation of the investment or investment course of action. *See* 85 FR at 72857 (Nov. 13, 2020).

[31] One commenter further warned that the rule could result in voter suppression, not just disenfranchisement, by preventing shareholders from reaching a quorum, which the Department itself acknowledged in the proposal would result in economic detriment to ERISA plans' holdings. Some corporate bylaws, for example, require a supermajority for certain votes, which may be difficult to achieve if certain shareholders are discouraged from voting.

fiduciary has a prudent process for proxy voting and other exercises of shareholder rights is a more workable framework for achieving the objectives of the proposal. The final rule carries forward from the proposal a provision that requires plan fiduciaries, when deciding whether to exercise shareholder rights and when exercising such rights, including the voting of proxies, to carry out their duties prudently and solely in the interests of the plan participants and beneficiaries and for the exclusive purpose of providing benefits to participants and beneficiaries and defraying the reasonable expenses of administering the plan. Also similar to the proposal, but with some modifications in response to public comments, the final rule includes a list of principles that fiduciaries must comply with when making decisions on exercising shareholder rights, including proxy voting, in order to meet their prudence and loyalty duties under ERISA section 404(a)(1)(A) and (B), including duties to act solely in accordance with the economic interest of the plan and its participants and beneficiaries and 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 promote non-pecuniary benefits or goals unrelated to the financial interests of the plan's participants and beneficiaries. Finally, the final rule includes specific language to make clear that plan fiduciaries do not have an obligation to vote all proxies, as well as a safe harbor provision, modified from the proposal, pursuant to which plan fiduciaries may adopt proxy voting policies and parameters prudently designed to serve the plan's economic interest that provide optional means for satisfying their fiduciary responsibilities regarding determining whether to vote under ERISA sections 404(a)(1)(A) and 404(a)(1)(B).

2. Elimination of Paragraphs (e)(3)(i) and (ii) From the Proposal

The principles-based approach adopted in the final rule is reflected by the Department's elimination of paragraphs (e)(3)(i) and (ii) from the proposal. Paragraph (e)(3)(i) of the proposal provided that a plan fiduciary *must* vote any proxy where the fiduciary prudently determined that the matter being voted upon would have an economic impact on the plan after considering those factors described in paragraph (e)(2)(ii) of the proposal and taking into account the costs involved (including the cost of research, if necessary, to determine how to vote). Paragraph (e)(3)(ii) of the proposal provided that a plan fiduciary must *not* vote any proxy unless the fiduciary prudently determined that the matter being voted upon would have an economic impact on the plan after considering those factors described in paragraph (e)(2)(ii) of the proposal and taking into account the costs involved.

The Department received a number of comments suggesting removal of the requirements in paragraphs (e)(3)(i) and (ii). Commenters criticized these provisions of the proposal as requiring a fiduciary to undertake an economic impact analysis in advance of each issue that is the subject of a proxy vote in order to even consider voting. A commenter further noted that a fiduciary may not discover until after the analysis is performed that the cost involved in determining whether to vote outweighs the economic benefit to the plan. Another commenter characterized this as a ''high risk compliance dilemma'' that could not be resolved without expending funds on analysis and documentation, without knowing in advance whether the expenditure is allowable. Commenters further indicated that the proposal was unclear as to how to establish whether an economic basis would be strong enough to justify voting and that it can be difficult, if not impossible, to ascertain whether a matter will have a future economic impact. Commenters further stated that the criteria enumerated in paragraph (e)(2)(ii) of the proposal for determining the economic impact of a proxy vote were too narrow, which could result in potentially negative consequences to plans because paragraph (e)(3)(ii) of the proposal could prohibit fiduciaries from engaging in activities that would mitigate risk. For instance, a commenter stated that, in its experience, once an evaluation of a proxy matter has been done, a situation with ''no economic impact'' is more of a theoretical possibility than a reality. According to this commenter, either its research will show that the matter being voted on will strengthen the company if implemented, or that it will not. The commenter further explained that, at a base level, a matter that would strengthen or otherwise improve a company is likely to result in an economic benefit in connection with a plan's investment when considered in the long-term. If a matter would not result in a net positive to the company, the commenter believes a fiduciary should vote against the proposal, not decline to vote. The commenter cautioned that prohibiting fiduciaries from voting in circumstances where they otherwise would vote against a matter may have the unintended consequence of allowing more frivolous proxy matters to be approved, resulting in decreased corporate accountability. Commenters also raised practical issues with respect to an obligation to *not* vote. Some explained that failing to vote can have the effect of a ''no'' vote or a ''yes'' vote, depending on the circumstances. Another commenter stated that modern proxy voting processes do not allow a holder of securities subject to the proxy to vote on some but not all proposals.

Other commenters, however, supported paragraph (e)(3)(ii) of the proposal. They viewed the provision as an important clarification that plan fiduciaries are not required to vote all proxies, which could reduce diversion of plan resources by restricting voting activity only to those issues that offer an economic benefit to the plan.

The Department has decided not to include the requirements in paragraphs (e)(3)(i) and (ii) of the proposal in the final rule at this time. The Department recognizes the concerns expressed by commenters regarding potentially increased costs and liability exposure, as well as the difficulty in some circumstances of determining whether a matter would have an economic impact and the possibility that a fiduciary might prudently determine that there are risks to plan investments that could result from not voting even when the matter being voted upon itself would not have an economic impact. Instead, the Department has provided a specific provision in the final rule stating that plan fiduciaries are not required to vote all proxies.

3. Section-by-Section Overview of Final Rule

(i) Paragraph (e)(1)

Paragraph (e)(1) of the final rule, like the proposal, provides that the fiduciary duty to manage plan assets that are shares of stock includes the management of shareholder rights appurtenant to the shares, such as the right to vote proxies. Commenters raised a number of issues with respect to the general scope of fiduciaries' responsibilities and obligations under the rule as set forth in paragraph (e)(1) of the proposal.

Several commenters supported the Department's goal of making clear that plan fiduciaries are not obligated to vote all proxies, and suggested the rule could be improved by including that clear statement in the regulatory text in paragraph (e)(1). The Department was clear in the preamble to the proposed rule that one objective of the proposal was to correct a misunderstanding among some fiduciaries and other stakeholders that ERISA requires every proxy to be voted. Thus, the Department agrees that it would be appropriate to include an explicit statement to that effect in the final rule. The Department, however, believes that the statement fits better in paragraph (e)(2) (regarding the principles that must be considered in deciding whether to exercise shareholder rights) and has added a statement to paragraph (e)(2)(ii) that the ERISA fiduciary duty to manage proxy voting and other shareholder rights does not require the voting of every proxy or the exercise of every shareholder right.

A commenter suggested that the rule should focus only on proxy voting, including the decision of whether to exercise voting rights, but should not extend to ''other shareholder rights.'' This commenter explained that other shareholder rights, such as inspecting an issuer's corporate record books and participating in corporate actions taken by the issuer, are substantively separate and distinct from proxy voting. Also, decisions on corporate actions such as stock splits, tender offers, exchange offers on bond issues, and mergers and acquisitions generally are not governed by proxy voting policies or undertaken with advice from proxy voting advisors. On this basis, the commenter recommended removing other shareholder rights from the rule. The Department is not persuaded to make the suggested change. The exercise of shareholder rights has been part of the Department's prior guidance since the first Interpretive Bulletin in 1994.[32] The Department believes that the exercise of shareholder rights to monitor or influence management, which may occur in lieu of, or in connection with, formal proxy proposals is just as much an issue of fiduciary management of the investment asset as proxy voting and accordingly should be covered by the final rule.

Commenters also requested clarifications related to plan investments in SEC-registered investment companies, such as mutual funds. Several commenters noted that the preamble to the proposal suggested that the rule would not apply to a mutual fund's exercise of shareholder rights with respect to the stock it holds, and requested that the Department provide confirmation. As previously explained, ERISA does not govern the management of the portfolio internal to an investment fund registered with the SEC, including such fund's exercise of its shareholder rights appurtenant to the portfolio of stocks it holds.[33] Accordingly, the final rule would not apply to such a fund's exercise of shareholder rights.

A commenter requested further clarification that the Department does not intend that plan fiduciaries apply the standards of the rule in reviewing, analyzing, or making a judgment on the proxy voting practices of the mutual funds in which the plan invests. This commenter explained that SEC-registered funds have the scale, internal expertise, and experience to analyze and vote proxies. According to the commenter, they also publicly report their proxy votes to the SEC, and must describe in their registration statements the policies and procedures that they use to determine how to vote proxies for their portfolio of securities. In the commenter's view, placing an obligation on plan fiduciaries to review and make judgments on the proxy voting practices of mutual funds in which they invest will substantially increase the administrative burden and costs for plans that invest in mutual funds. In contrast, another commenter suggested that the final rule should require fiduciaries to investigate a mutual fund's objectives in shareholder voting and engagement with portfolio companies and determine that the objectives are consistent with ERISA's loyalty requirement prior to deciding to invest in the fund or considering it as an option for participants. The commenter noted that since the issuance of the Avon Letter, plans increasingly invest in mutual funds or exchange-traded funds (ETFs) with stock voting authority residing in the funds. This commenter argued that nothing in the Avon Letter or subsequent guidance from the Department suggested that ERISA absolves a plan investment fiduciary of any fiduciary duty associated with the shareholder voting of shares that it owns indirectly through its share ownership in mutual funds and ETFs.

In response to these comments, the Department notes that the issue raised by these commenters is beyond the scope of this rulemaking. Rather, fiduciary responsibilities with respect to investment decisions are addressed in the other provisions of the Investment Duties regulation, as recently amended. Paragraph (c)(1) provides that, in general, a fiduciary's evaluation of an investment or investment course of action must be based only on pecuniary factors and that a fiduciary may not subordinate the interests of participants and beneficiaries in their retirement income or financial benefits under the plan to other objectives and may not sacrifice investment return or take on additional investment risk to promote non-pecuniary benefits or goals. Furthermore, the weight given to any pecuniary factor by a fiduciary should appropriately reflect a prudent assessment of its impact on risk and return. Whether a particular fund's proxy voting activities would constitute a pecuniary factor and, if so, how much weight it should be given in an investment decision, are factual questions that should be resolved by the responsible fiduciary based on surrounding circumstances.

Some commenters requested clarification of whether the rule applies to plan fiduciaries in the exercise of shareholder rights with respect to mutual funds and ETFs (which are sometimes organized as corporate or similar entities) when the fund itself seeks a vote of its shareholders on fund matters. According to commenters, for a variety of reasons, SEC-registered funds often face more challenges than operating companies to achieve a quorum and obtain approval of their proxy matters. The commenters explained that this is due to major differences in shareholder bases (funds have more diffuse and retail-oriented shareholder bases), proxy voting behavior of those bases (institutional investors comprise a larger percentage of operating companies' shareholder bases and are far more likely to vote), legal obligations, and organizational differences.

Furthermore, according to commenters, funds also can have difficulty even identifying and reaching their shareholders when they invest through intermediaries, which severely limits a fund's ability to communicate with its shareholders to encourage voting. These factors contribute significantly to the costs and efforts required to seek and obtain necessary shareholder approvals for fund matters. Funds, and therefore fund shareholders, often bear the proxy costs associated with proxy campaigns, including costs associated with follow-up solicitations.

According to a commenter, the SEC has recognized these issues in recent years. The commenter, as well as others, expressed concern that the rule could create further difficulty for funds in carrying out their proxy campaigns and potentially result in imposing unnecessary costs on funds, particularly in connection with funds' ability to

[32] *See* 59 FR 38860, 38864 (July 29, 1994) (discussing activities to monitor or influence management by variety of means including by exercise of legal rights of a shareholder).

[33] 85 FR 55219, 55234 (Sept. 4, 2020).

achieve a timely quorum at their own shareholder meetings. Another commenter indicated that ERISA plan investors receive a variety of proxies that must be evaluated, not only in connection with shares of common stock held by the plan, but also from SEC-registered funds as well as bank collective trust funds and other collective funds in which plans invest. The commenter stated that the regulated community needs to be able to clearly identify those proxies that are subject to the rule and those that are not. The commenter requested that the rule itself provide that plan investments in such securities are not subject to the requirements of the rule.

In the proposal, the Department recognized that the proposed rule could impact the ability to achieve a quorum at shareholder meetings of funds.[34] The Department believes that the changes made to the final rule significantly eliminate any provisions of the proposal that might impede achieving a quorum for shareholder meetings, including those held by funds. Under the proposal, a fiduciary would have not been able to vote unless the fiduciary prudently concluded that the matter being voted upon would have an economic impact on the plan. The burden of determining whether a fiduciary must, or must not, vote under the proposal was likely to result in fiduciaries opting to refrain from voting under one of the permitted practices described in the proposal. The Department's removal of the ''vote/not vote'' determination from the final rule should eliminate any concerns with potential liability on a fiduciary associated with making an incorrect decision as to whether or not to cast a proxy vote. The safe harbors in the final rule are also sufficiently flexible to permit a fiduciary to adopt voting policies that would permit proxy voting for fund shares while refraining from voting other types of shares. Moreover, the Department continues to believe, as stated in the preamble to the proposal, that fiduciary proxy voting policies may consider the economic detriment to a plan's investment that might result from direct and indirect costs incurred related to delaying a shareholders' meeting.[35]

(ii) Paragraph (e)(2)

Paragraph (e)(2) of the proposal set forth the general responsibilities with respect to the exercise of shareholder rights under the regulation, and stated that when deciding whether to exercise shareholder rights and when exercising such rights, including the voting of proxies, fiduciaries must carry out their duties prudently and solely in the interests of the participants and beneficiaries and for the exclusive purpose of providing benefits to participants and beneficiaries and defraying the reasonable expenses of administering the plan pursuant to ERISA sections 403 and 404.

Paragraph (e)(2)(i)

A commenter noted that paragraph (e)(2)(i) of the proposal referenced ERISA sections 403 and 404, and because those two separate sections each carry separate responsibilities, suggested that each be designated as a separate clause in the final regulation because a fiduciary could breach or fulfill one but not the other. The Department recognizes the separate responsibilities under sections 403 and 404 of ERISA, but has decided to remove the reference to section 403 for paragraph (e)(2)(i) of the final rule. As explained in connection with recently adopted amendments to the Investment Duties regulation, the Department believes it is important that the regulation focus on section 404 of ERISA.[36] Although similar, and although actions taken in compliance with section 404 would likely satisfy similar obligations under section 403, the text of ERISA section 403 is not identical to ERISA section 404(a)(1)(A), and the Department is wary of possible inferences that compliance with the provisions of the final rule would also necessarily satisfy all the provisions of ERISA section 403. The Department also believes explicit reference to ERISA section 404 is not necessary because paragraph (e) is part of 29 CFR 2550.404a–1. As a result, paragraph (e)(2)(i) of the final rule provides that when deciding whether to exercise shareholder rights and when exercising such rights, including the voting of proxies, fiduciaries must carry out their duties prudently and solely in the interests of the participants and beneficiaries and for the exclusive purpose of providing benefits to participants and beneficiaries and defraying the reasonable expenses of administering the plan.

Activities that are intended to monitor or influence the management of corporations in which the plan owns stock can be consistent with a fiduciary's obligations under ERISA, if the responsible fiduciary concludes that such activities (by the plan alone or together with other shareholders) are appropriate after applying the considerations set forth in the final rule. However, the use of plan assets by fiduciaries to further policy-related or political issues, including ESG issues, through proxy resolutions would violate the prudence and exclusive purpose requirements of ERISA sections 404(a)(1)(A) and (B) and the final rule unless such activities are undertaken solely in accordance with the economic interests of the plan and its participants and beneficiaries. The mere fact that plans are shareholders in the corporations in which they invest does not itself provide a rationale for a fiduciary to spend plan assets to pursue, support, or oppose such proxy proposals. Moreover, the use of plan assets by fiduciaries to further policy or political issues through proxy resolutions that are not likely to enhance the economic value of the investment in a corporation would, in the view of the Department, violate the prudence and exclusive purpose requirements of ERISA sections 404(a)(1)(A) and (B) as well as the final rule. For example, with respect to proposals submitted by shareholders that request a corporation to incur costs, either directly or indirectly, without the proposal including a demonstrable expected economic return to the corporation, a fiduciary may, depending on the facts and circumstances, be obligated under ERISA and the final rule to vote against such proposals in order to protect the financial interests of the plan's participants and beneficiaries.[37] Similarly, in the Department's view, it would not be appropriate for plan fiduciaries, including appointed investment managers, to incur expenses to engage in direct negotiations with the board or management of publicly held companies with respect to which the plan is just one of many investors. Nor generally should plan fiduciaries fund advocacy, press, or mailing campaigns on shareholder resolutions, call special shareholder meetings, or initiate or actively sponsor proxy fights on environmental or social issues relating to such companies, unless the responsible plan fiduciary concludes that such activities (alone or together with other shareholders) are appropriate

[34] Id. at 55234.

[35] Id. at 55226.

[36] 85 FR 72846, (Nov. 13, 2020).

[37] The Department is not suggesting that a fiduciary must perform its own economic analysis, or incur expenses to obtain an analysis, to determine whether the proposal will economically benefit the corporation and its shareholders. For example, a fiduciary could prudently consider a credible economic analysis provided by the shareholder proponent.

after applying the considerations set forth in the final rule.[38]

Paragraph (e)(2)(ii)

Paragraph (e)(2)(ii) of the proposal set forth specific standards for fiduciaries to meet when deciding whether to exercise shareholder rights and when exercising shareholder rights. The requirements in paragraph (e)(2)(ii) of the proposal also served as the basis for a fiduciary's determination of whether a matter being voted upon would have an economic impact on a plan for purposes of compliance with paragraph (e)(3) of the proposal. Many commenters focused specifically on paragraphs (e)(2)(ii)(A) and (B) of the proposal, which required, in relevant part, that fiduciaries (A) consider 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, and (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.

Some commenters argued that the specificity of the proposal did not comport with what they asserted was a congressional intent that eschewed a prescriptive approach to ERISA's duties of loyalty and prudence, or with the Department's own Investment Duties regulation. Commenters also noted the potential burdens that paragraph (e)(2)(ii) of the proposal would place on plan fiduciaries to evaluate and justify decisions for potentially large numbers of proxy proposals and to monitor an investment manager's or proxy advisory firm's voting policy for consistency with the regulation, which could result in increased costs that would ultimately be borne by plan participants. Commenters also stated that the provision's requirement to take into account plan-specific factors did not adequately recognize that investment managers do not have information on plan holdings they do not directly manage. Commenters further indicated that, with a focus on individual plans as opposed to investment managers responsible for pools of plan assets, paragraph (e)(2)(ii)(B) of the proposal failed to consider situations when several ERISA plans, particularly those with aligned objectives and liabilities, may together hold a significant stake in a company. In such cases, voting together could impact the investment and, as a result, each investor's portfolio. They argued that the proposal, in contrast, potentially would result in proxies being un-voted if each ''slice'' of the aggregate is too insignificant.

A commenter further suggested that an economic impact test, as described in the proposal, was ill-suited to the purpose and role of proxy voting. According to the commenter, many of the items on which corporate law permits shareholders to have a say—for example, the election of directors or ratification of auditors—are to mitigate risk and assure prophylactic measures are in place to avoid threats to their share of capital over the long term. The commenter questioned how a fiduciary would determine that voting against a company-proposed director for election to the board who was clearly unqualified and incompetent would have an economic impact on the plan. Another commenter explained that some votes, such as those supporting good corporate governance practices (*e.g.,* election of outside directors) may not have an immediate measurable economic effect, but still be in the interest of plan investors. Another commenter opined that a short-term economic impact will be easier to prove or disprove in terms of share price or other similarly rudimentary indicators, but questioned whether the rule should encourage fiduciaries to think only in terms of short-term economic gains. In this regard, several commenters requested that the Department confirm that a fiduciary may take into consideration the long-term nature of a plan's investment horizon. A commenter also suggested that the Department expand the criteria for voting to include issuer risk-based factors that ''promote long-term growth and maximize return on ERISA plan assets.'' Another commenter explained that proposals that encourage greater disclosure can result in enhancing shareholder value or serve in a prophylactic manner to prevent actions that might serve to diminish shareholder value. A commenter also criticized the proposal as focusing on the impact on individual plan investments. Commenters explained that modern portfolio theory focuses on the role that an investment plays in the context of an overall portfolio rather than on a stand-alone basis, and expressed the view that the roles that proxy voting and shareholder voices play in current portfolio risk management practices should be evaluated in the context of the long-term and portfolio-wide strategy, with consideration of the aggregate effects of shareholder votes and voices.

After considering these comments, the Department has modified paragraph (e)(2)(ii)(A) and (B). An important goal in proposing the rule was to ensure that in making proxy voting decisions, fiduciaries act for the exclusive purpose of financially benefitting plan participants and not subordinating the interests of the plan and its participants to goals and objectives unrelated to their financial interests. Recent amendments to the Investment Duties regulation, which applies generally to fiduciary decisions on investments and investment courses of action, were adopted for much the same purpose.

Paragraph (e)(2)(ii)(A) of the final rule requires that, when deciding whether to exercise shareholder rights and when exercising shareholder rights, a fiduciary must act solely in accordance with the economic interest of the plan and its participants and beneficiaries. The proposed requirement to prudently determine whether the economic value of the plan's investment will be affected based on a determination of risk and return over an appropriate investment horizon has not been included in the final rule in order to address commenter concerns that the impact of proxy voting may not be readily quantifiable and to reduce potential compliance costs. In the Department's view, the final rule provides sufficient flexibility for fiduciaries to consider longer-term consequences and potential economic impacts. Further, removal of the references to a plan's investment objectives and funding policy responds to concerns that investment managers responsible for only a portion of the plan assets may have limited access and visibility into those objectives and funding policies and such considerations may unnecessarily increase compliance costs without a commensurate benefit for the plan or its participants.

The Department, however, cautions fiduciaries from applying an overly expansive view as to what constitutes an economic interest for purposes of paragraph (e)(2)(ii)(A) of the final rule. As previously discussed, the costs incurred by a corporation to delay a shareholder meeting due to lack of a quorum is an example of a factor that can be appropriately considered as affecting the economic interest of the plan. However, vague or speculative

[38] Although the provision in the proposal also made reference to ''purposes of the plan,'' the language is not carried forward in the final provision as the Department believes it is unnecessary because the purposes of a plan would be encompassed by the financial interests of plan participants and beneficiaries.

notions that proxy voting may promote a theoretical benefit to the global economy that might redound, outside the plan, to the benefit of plan participants would not be considered an economic interest under the final rule.

Paragraph (e)(2)(ii)(B) of the proposal required consideration of 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, and the plan's percentage ownership of the issuer. Similar to the changes made to paragraph (e)(2)(ii)(A) of the final rule, the Department has removed this language to address concerns that where portions of the portfolio are managed by different investment managers, a specific manager may not know the plan's overall aggregate exposure to a single issuer. Accordingly, paragraph (e)(2)(ii)(B) of the final rule has been revised only to require a fiduciary consider the impact of any costs involved. However, in the Department's view, where the plan's overall aggregate exposure to a single issuer is known, the relative size of an investment within a plan's overall portfolio and the plan's percentage ownership of the issuer, may still be relevant considerations in appropriate cases in deciding whether to vote or exercise other shareholder rights.

Several commenters requested further guidance or examples of costs that a fiduciary would be required to consider. In the view of the Department, for purposes of paragraph (e)(2)(ii)(B) of the final rule, the types of relevant costs would depend on the particular facts and circumstances. Such costs could include direct costs to the plan, including expenditures for organizing proxy materials; analyzing portfolio companies and the matters to be voted on; determining how the votes should be cast; and submitting proxy votes to be counted. If a plan can reduce the management or advisory fees it pays by reducing the number of proxies it votes on matters that have no economic consequence for the plan that also is a relevant cost consideration. In some cases, voting proxies may involve out-of-the-ordinary costs or unusual requirements, such as may be the case of voting proxies on shares of certain foreign corporations. Opportunity costs in connection with proxy voting could also be relevant, such as foregone earnings from recalling securities on loan or if, as a condition of submitting a proxy vote, the plan will be prohibited from selling the underlying shares until after the shareholder meeting.

Paragraph (e)(2)(ii)(C) of the proposal provided that a fiduciary must 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 these financial interests of the plan's participants and beneficiaries or the purposes of the plan. A commenter took issue with this requirement, suggesting that it was inconsistent with some client expectations, as well as stewardship codes outside the United States that do not limit significant votes to economic impact to the portfolio. The Department disagrees and notes that the provision reflects the fundamental fiduciary duty of loyalty as set forth in ERISA section 404(a)(1)(A). The Department has modified the final rule in order to avoid suggesting that a fiduciary may exercise proxy voting and other shareholder rights with the goal of advancing non-pecuniary goals unrelated to the financial interests of the plan's participants and beneficiaries so long as it does not result in increased costs to the plan or a decrease in value of the investment. Thus, paragraph (e)(2)(ii)(C) of the final rule states that a fiduciary must 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 promote non-pecuniary benefits or goals unrelated to these financial interests of the plan's participants and beneficiaries.

Paragraph (e)(2)(ii)(D) of the proposal provided that a fiduciary must investigate material facts that form the basis for any particular proxy vote or other exercise of shareholder rights. The provision further stated that 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, as defined in paragraph (e)(2)(ii)(A) of the proposal.

A commenter suggested the provision's requirement to investigate material facts was overly broad, and explained that there may be instances when routine or recurring proxy votes, such as annual proxy votes on the same subject, may not require a separate and distinct investigation in order for a fiduciary to make a prudent determination. A commenter indicated that paragraph (e)(2)(ii)(D) is overly burdensome, and that issues are addressed in paragraphs (e)(2)(ii)(F) and (e)(2)(iii) (relating to selection of service providers and delegation to investment managers). The commenter recommended deletion of the provision.

On the other hand, another commenter suggested that the Department go further with the fiduciary requirement to investigate material facts by explicitly referencing review of the issuer response statements required by recently-adopted SEC proxy solicitation rules. The commenter indicated these filings may include significant, material information that could impact a voting decision (including decisions about whether to vote and how to vote) that by definition would not be considered by the proxy advisory firm in drafting its recommendation. Additionally, according to the commenter, recent SEC guidance on the proxy voting responsibilities of investment advisers encourages investment advisers to have policies and procedures in place to consider the information available to them about proxy advisory firms themselves under the SEC's new proxy solicitation rules (*e.g.,* disclosures of proxy advisory firm conflicts of interests) as well as any information that comes to light after they have received a proxy advisory firm's voting recommendations (*e.g.,* additional soliciting material setting forth an issuer's views on a recommendation). The supplemental guidance further states that, under certain circumstances, an investment adviser would likely need to consider such additional information from an issuer prior to exercising voting authority in order to demonstrate that it is voting in its client's best interest, and that it should disclose how its policies and procedures address the use of automated voting in cases where it becomes aware before the submission deadline for proxies that an issuer intends to file or has filed additional soliciting materials regarding a matter to be voted upon.

Several commenters raised a number of concerns in connection with paragraph (e)(2)(ii)(D) of the proposal about proxy advisory firms, including conflicts of interest resulting from business relationships with companies that are the subject of proxy recommendations, a ''one-size-fits-all'' approach to corporate governance that does not take into account differences in companies' business models, a lack of transparency in the process by which proxy advisory firm recommendations are developed, errors in proxy advisory firm reports and recommendations, proxy advisory firms' resistance to engaging in a dialogue with issuers to correct errors and misunderstandings, automatic submission of votes for clients, cutting plan managers out of the decision-making process, and depriving issuers of a chance to correct the record or provide the market with additional information.

After considering the comments, the Department is modifying paragraph (e)(2)(ii)(D) by requiring a fiduciary to evaluate, rather than investigate, material facts. This change is to remove any implication that plan fiduciaries would be expected to conduct their own investigation of material facts, which was not intended by the Department. Instead, the intent of this provision was to ensure that in making informed proxy voting decisions, fiduciaries should consider information material to a matter that is known or that is available to and reasonably should be known by the fiduciary. In this regard, the Department notes that, as described by the commenter above, as a result of recent SEC actions, clients of proxy advisory firms may become aware of additional information from an issuer which is the subject of a voting recommendation.[39] An ERISA fiduciary would be expected to consider the relevance of such additional information if material. Paragraph (e)(2)(ii)(D) of the final rule thus provides that a fiduciary must evaluate material facts that form the basis for any particular proxy vote or other exercise of shareholder rights.

Some commenters also suggested that the Department strengthen the rule by including specific regulatory text that generally disallows ''robovoting,'' a term some commenters describe as automatic voting mechanisms relying on proxy advisors. A commenter questioned whether robovoting is consistent with ERISA's stringent standards. Another commenter suggested that robovoting is an abridgment of fiduciary responsibility. Some commenters also suggested that the Department should prohibit robovoting for significant, contested, and controversial proxy votes. Commenters also suggested that the Department consider placing conditions on the use of robovoting, such as allowing robovoting only if a company that is the subject of a proxy advisory firm's recommendations has not submitted a response to the recommendation.

The Department intended that the provisions in paragraph (e)(2)(ii)(D) of the proposal address the sort of concerns raised by these comments and provide appropriate guidelines for ERISA fiduciaries. The provision in the proposal stated, in relevant part, that a 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 as defined in paragraph (e)(2)(ii)(A) of the proposal. The Department does not dispute that proxy advisory firms can play a role in providing information to fiduciaries and economizing investors' ability to exercise shareholder rights and proxy voting. However, public comments submitted in connection with the proposal, and recent SEC actions in this area described above, highlight aspects of the proxy advisory firms' recommendations and services that can be problematic in a variety of ways. For example, the Department acknowledges some commenters noted that many ERISA plans rely on proxy advisory firms' pre-population and automatic submission mechanisms for proxy votes, which can provide a cost-effective way to exercise their shareholder voting rights in cases where the proxy advisor has processes which assure that its voting recommendations conform to the obligations that plan managers hold as fiduciaries. However, adopting such a practice for all proxy votes effectively outsources their fiduciary decision-making authority. Rather, as the Department noted in the preamble to the proposed rule, ''certain proposals may require a more detailed or particularized voting analysis.''[40]

In light of other changes in paragraph (e)(2) intended to adopt a more principles-based approach in the final rule, the Department has concluded that it would be better to address these proxy advisory firm issues in a separate paragraph in the final rule, which is described under paragraph (e)(2)(iv).

Paragraph (e)(2)(ii)(E) of the proposal required a fiduciary to 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. Recognizing that ERISA's prudence obligation carries with it a requirement to maintain records and document fiduciaries' decisions, most commenters did not seriously object to the proposal's general obligation to maintain records on proxy voting activities and other exercises of shareholder rights. Commenters did, however, express concern that the proposal included particularized recordkeeping mandates that were both unnecessary and costly. One commenter suggested an alternative that fiduciaries must make prudent efforts to maintain accurate records that include proxy voting activities and, where authority is delegated, require the same of that person. Other commenters complained that the requirement to maintain specific records demonstrating the basis for particular votes was unnecessary and costly. Some commenters observed that such a level of recordkeeping would exceed that required for other potentially more impactful investment decisions. Another noted that the provision appeared to require a level of recordkeeping greater than described in current guidance, and complained that the Department did not adequately explain the reason for this change. The commenter noted that the Department stated in 2011 that there was no basis to impose more onerous documentation requirements that treat proxy voting differently from other fiduciary activities.[41] Some commenters requested general clarification on the types of documents that would be necessary to demonstrate the basis for a vote. A commenter suggested a specific clarification that proxy voting activity that is consistent with an applicable proxy voting policy does not require additional explanation or documentation. Further, as discussed below, commenters expressed concern that the requirement in paragraph (e)(2)(ii)(E) of the proposal to maintain documents demonstrating the basis for particular votes, as well as a similar requirement in paragraph (e)(2)(iii) of the proposal (relating to delegation of responsibilities to investment managers), suggested that the proposal would create new and heightened monitoring obligations for fiduciaries

[39] 2020 SEC Supplemental Guidance, 85 FR at 55155–57. Fiduciaries may retain proxy advisory firms and other service providers, subject to any applicable requirements of paragraphs (e)(2)(ii)(F) and (e)(2)(iii) and (iv), as part of satisfying the fiduciaries' obligations to evaluate material facts.

[40] 85 FR at 55224. The SEC 2019 Guidance for Investment Advisers similarly cautioned that a higher degree of analysis ''may be necessary or appropriate'' for certain types of matters, including corporate events such as mergers and acquisitions, or matters that are ''highly contested or controversial.'' *Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers,* 84 FR 47420, 47423–24 (Sept. 10, 2019). Release Nos. IA–5325; IC–33605, *available at www.govinfo.gov/content/pkg/FR-2019-09-10/pdf/2019-18342.pdf.*

[41] *See* Dep't of Labor Office of Inspector Gen. Report No. 09–11–001–12–121 (March 31, 2011). The commenter cited the EBSA response to OIG conclusion that EBSA does not have adequate assurances that fiduciaries or third parties voted proxies solely for the economic benefit of plans.

that delegate responsibilities to investment managers.

It has long been the view of the Department that compliance with the duty to monitor necessitates proper documentation of the activities that are subject to monitoring. However, the Department agrees that a less prescriptive approach to recordkeeping obligations is appropriate. The Department is retaining the general recordkeeping requirement, but is removing the requirement to maintain documents that would be necessary to demonstrate the basis for a vote to avoid any inferences related to responsibilities in monitoring investment managers, which are addressed in paragraph (e)(2)(iii) of the final rule. Thus, paragraph (e)(2)(ii)(E) of the final rule requires fiduciaries to maintain records on proxy voting activities and other exercises of shareholder rights. In general, the extent of the documentation needed to satisfy the monitoring obligation will depend on individual circumstances, including the subject of the proxy voting and its potential economic impact on the plan's investment. For fiduciaries that are SEC-registered investment advisers, the Department intends that the recordkeeping obligations under paragraph (e)(2)(ii)(E) be applied in a manner that aligns to similar proxy voting recordkeeping obligations under the Advisers Act.[42]

Paragraph (e)(2)(ii)(F) of the proposal required that fiduciaries exercise prudence and diligence in the selection and monitoring of persons, if any, selected to advise or otherwise assist with exercises of shareholder rights, such as providing research and analysis, recommendations regarding proxy votes, administrative services with voting proxies, and recordkeeping and reporting services.

Various commenters supported the Department's effort to better regulate proxy advisory firms and the proxy advisory process and suggested additional steps the Department should take in a final rule. Some suggested mandating disclosure of fees paid by investment managers to proxy voting advisors, prohibiting proxy advisory firms from consulting with companies when they also make recommendations on voting issues for that company, and establishing a baseline disclosure standard to which all proxy voting advice businesses must adhere. Others suggested placing specific conditions on a fiduciary's ability to rely on a proxy advisory firm's voting recommendation, such as requiring the proxy advisory firm to demonstrate that it had researched and analyzed evidence that would support a conclusion contrary to the proxy advisory firm's conclusion. A commenter suggested that the Department should make more specific reference to proxy advisory firm conflict of interest disclosures required by the recently amended SEC proxy solicitation rules. According to the commenter, the SEC rules require that proxy advisory firms provide specific, prominent disclosures of their conflicts of interest and of any policies and procedures designed to mitigate said conflicts. Additionally, these disclosures must be specific to the company on which the proxy advisory firm is issuing a report. The commenter recommended that the fiduciaries should be required to review a proxy advisory firm's conflicts disclosure, and that the Department should caution ERISA fiduciaries against relying on a proxy advisory firm's recommendations if the disclosures reveal a conflict with respect to an issuer that calls into question the firm's ability to provide objective advice. Another commenter suggested that the Department should wait until implementation of the SEC's new regulations to determine if any further action is necessary, and that the Department's approach to regulating fiduciary use of proxy advisory firms should align with the approach taken by the SEC so that SEC-registered investment advisers are subject to a consistent standard regarding their use of proxy advisory firms. On the other hand, some commenters criticized the Department's focus on proxy advisory firms as being based on unsupported allegations of proxy advisory firm critics, without the Department either substantiating those criticisms or noting the self-interest of the persons making those allegations.

After considering the public comments, the Department is adopting paragraph (e)(2)(ii)(F) in the final rule unmodified. It provides that fiduciaries must exercise prudence and diligence in the selection and monitoring of persons, if any, selected to advise or otherwise assist with exercises of shareholder rights, such as providing research and analysis, recommendations regarding proxy votes, administrative services with voting proxies, and recordkeeping and reporting services. The provision is essentially a restatement of the general fiduciary obligations that apply to the selection and monitoring of plan service providers, articulated in the context of fiduciary and other service providers that advise or assist with exercises of shareholder rights. Thus, as a general matter, fiduciaries will be expected to assess the qualifications of the provider, the quality of services offered, and the reasonableness of fees charged in light of the services provided. The process also must avoid self-dealing, conflicts of interest or other improper influence. In considering any proxy recommendation, fiduciaries should assure that they are fully informed of potential conflicts of proxy advisory firms and the steps such firms have taken to address them. Furthermore, to the extent applicable, fiduciaries will be expected to review the proxy voting policies and/or proxy voting guidelines and the implementing activities of the person being selected. If a fiduciary determines that the recommendations and other activities of such person are not being carried out in a manner consistent with those policies and/or guidelines, then the fiduciary will be expected to take appropriate action in response.

A commenter suggested deleting the list of services related to proxy voting. The commenter explained that the list is incomplete, and that codifying it might create confusion as to the types of services that may be necessary or appropriate for a particular voting activity. The Department does not believe it necessary to modify the provision as it is clear that the provision is not attempting to limit in any way the types of services that a plan or plan fiduciary may utilize in connection with exercising shareholder rights. Also, although the Department agrees that it would be important for a fiduciary to consider the proxy advisory conflict of interest disclosure required under recent SEC guidance, and that a fiduciary should consider whether potential conflicts may affect the quality of services to be provided, the Department does not believe it appropriate to expressly require review of such disclosure in paragraph (e)(2)(ii)(F) of the final rule because the provision could become outdated as disclosure obligations change over time. Rather, the Department believes that a general principles-based provision is adequate and would require ERISA fiduciaries to review disclosures of conflicts of interest required by SEC rules or guidance.

Paragraph (e)(2)(iii)

Paragraph (e)(2)(iii) of the proposal required that, where the authority to vote proxies or exercise shareholder rights has been delegated to an investment manager pursuant to ERISA section 403(a)(2), or a proxy voting firm or other person performs advisory services as to the voting of proxies, a responsible plan fiduciary must require

[42] *See infra* note 43 and accompanying text.

such investment manager or proxy advisory firm 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. The preamble explained that the proposal required fiduciaries to require documentation of the rationale for proxy-voting decisions so that fiduciaries can periodically monitor those decisions.

Commenters expressed concern that paragraph (e)(2)(iii) of the proposal appeared to require a delegating fiduciary to, in effect, peer over the shoulder of an investment manager and supervise each voting decision to confirm the voting decision was made based on the economic impact on the plan. Commenters noted that such a monitoring obligation for proxy voting would be higher than for other fiduciary activities, and would be inconsistent with ERISA's general rules and prior Department guidance related to delegation of fiduciary responsibilities. Commenters asked for clarification that fiduciaries would not be required to monitor every proxy vote or second-guess other fiduciaries' specific proxy voting decisions, unless the fiduciary knows or should know the designated fiduciary is violating ERISA with their proxy voting procedures.

Another commenter recommended removal of the requirement that a fiduciary require its investment managers and proxy advisory firms to document each voting decision along with the rationale for each decision, indicating that it would create unmanageable liability risk for fiduciaries by suggesting an obligation to review every voting decision made. Commenters indicated that the documentation requirement would be costly for investment managers, believing they would need to justify and communicate their decisions regarding the benefit of each proxy agenda item to each plan client. Another commenter suggested industry practice is that, when votes are exercised in accordance with approved proxy voting guidelines generally, only votes contrary to approved guidelines warrant specific documentation. Other commenters, however, believed documentation would be beneficial in protecting plan interests and suggested that further access to information and analyses from proxy advisory firms would help plan fiduciaries understand how the advisory firms developed their recommendations.

The Department did not intend to create a higher standard for a fiduciary's monitoring of an investment manager's proxy voting activities than would ordinarily apply under ERISA with respect to the monitoring of any other fiduciary or fiduciary activity. Thus, the Department has revised the provision in the final rule to eliminate the requirement for documentation of the rationale for proxy voting decisions, and instead replaced it with a more general monitoring obligation. Specifically, paragraph (e)(2)(iii) of the final rule provides that where the authority to vote proxies or exercise shareholder rights has been delegated to an investment manager pursuant to ERISA section 403(a)(2), a proxy voting firm or other person who performs advisory services as to the voting of proxies, a responsible plan fiduciary shall prudently monitor the proxy voting activities of such investment manager or proxy advisory firm and determine whether such activities are consistent with paragraphs (e)(2)(i)–(ii) and (e)(3) of the final rule. The Department notes that while the provision does not contain a specific documentation requirement, an SEC rule requires investment advisers registered with the SEC under the Advisers Act to maintain a record of each proxy vote cast on behalf of a client, retain documents created by the adviser that were material to a decision on how to vote or that memorialize the basis for that decision, and to maintain each written client request for information on how the adviser voted proxies on behalf of the client and any written response by the investment adviser to any (written or oral) client request for information on how the adviser voted proxies on behalf of the requesting client.[43] These requirements may be helpful to responsible plan fiduciaries in fulfilling monitoring requirements under paragraph (e)(2)(iii).

Commenters also raised concerns about the statement in the preamble to the proposal that suggested uniform proxy policies may sometimes jeopardize responsible plan fiduciaries' satisfaction of their duties under ERISA as suggesting that ERISA plans should require investment managers to use customized policies. A commenter explained that currently investment managers with voting discretion may vote consistently across client accounts as appropriate (*i.e.,* on those proposals for which objectives of the accounts are consistent and divergent economic interests or client-specific preferences are not present). Similarly, another commenter indicated that many investment advisers registered with the SEC use consistent proxy voting policies across client accounts, including accounts held by ERISA plans and pooled investment vehicles, because they believe those policies are in the best interest of clients.

Some commenters believed that developing customized policies for particular ERISA plans or collective investment vehicles used by ERISA plans would increase costs for plans and investment managers without incremental benefit to participants and beneficiaries. A commenter noted that investment managers might need to run a parallel voting process for ERISA and non-ERISA assets, which would create additional administrative burden and costs. A commenter also asserted that due to increased risk, some managers might move in the direction of not undertaking voting responsibilities, which would then require plans to make their own assessments and invariably result in increased costs.

A commenter suggested that the proposal's approach to regulating fiduciary use of proxy advisory firms should align with the approach taken by the SEC so that SEC-registered investment advisers are subject to a consistent standard regarding their use of proxy advisory firms. A commenter noted similar concerns in the context of proxy advisory services, indicating that paragraph (e)(2)(iii) implied that proxy advisors must tailor their rationale for every recommendation to each specific plan (and its participants) whose asset manager uses its research. A commenter believed such a requirement would be unnecessarily plan specific and unworkable. The commenter explained that proxy advisory firms support their clients, such as asset managers to retirement plans, by providing recommendations based on their chosen proxy voting policy, which is usually a custom policy the asset manager has selected to serve the interest of its client (*e.g.,* a retirement plan and its participants). According to the commenter, the client's decisions as to what its policy should be and how it should vote are at the sole discretion of the asset manager.

With respect to uniform proxy policies being utilized by investment managers, it was not the Department's intention to suggest that plans must require investment managers to vote

[43] SEC Rule 204–2, 17 CFR 275.204–2; *see also* SEC Rule 206(4)–6(b) and (c), 17 CFR 275.206(4)–6(b) and (c) (relating to certain disclosures about proxy voting by an investment adviser that must be provided to, or may be requested by, a client of the investment adviser).

according to custom policies. Rather, the Department's statement reflected a general concern that responsible fiduciaries might be accepting investment managers' proxy voting policies without sufficient review as to whether those policies comply with ERISA and, if so, whether the investment managers were complying with those policies. The Department believes that the revisions to the recordkeeping requirement in the final rule described above appropriately address that issue.

Paragraph (e)(2)(iv)

In light of other changes in paragraph (e)(2) intended to adopt a more principles-based approach in the final rule, some provisions related to proxy advisory firms that were in paragraph (e)(2)(ii)(D) of the proposal have been moved to a new paragraph (e)(2)(iv) in the final rule. Specifically, paragraph (e)(2)(ii)(D) of the proposal stated that 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 as defined in paragraph (e)(2)(ii)(A) of the proposal.

Paragraph (e)(2)(iv) of the final rule generally includes the same fiduciary obligations with respect to the use of proxy advisory firms and other service providers that were described in paragraph (e)(2)(ii)(D) of the proposal, with some modifications to strengthen the oversight obligations of fiduciaries who retain proxy advisory firms or other service providers. In response to the public comments that cited fiduciary practices that carry a high risk of noncompliance with ERISA, paragraph (e)(2)(iv) of the final rule has been modified so that a fiduciary that chooses to follow the recommendations of a proxy advisory firm or other service provider must determine that the firm or service provider's proxy voting guidelines are consistent with the five factors set forth in paragraph (e)(2)(ii)(A)–(E) of the final rule, rather than only paragraph (e)(2)(ii)(A). Because paragraph (e)(2)(ii)(F) of the final rule covers the exercise of prudence and diligence in the selection and monitoring of proxy advisory firms and other service providers, it would not generally be applicable to the proxy voting guidelines of a proxy advisory firm or other service provider.

Paragraph (e)(2)(iv) of the final rule removes the appropriate supervision requirement since that requirement duplicates the monitoring obligations set forth in paragraph (e)(2)(ii)(F) of the final rule. A fiduciary that retains a proxy advisory firm or other service provider, however, remains subject to the prudence and diligence obligations described in paragraph (e)(2)(ii)(F) regarding the selection of that person and, if the fiduciary adopts a practice of following the recommendations of that person, the fiduciary is subject to the additional requirements of paragraph (e)(2)(iv) of the final rule.

(iii) Paragraph (e)(3)

Paragraphs (e)(3)(i) and (ii) of the proposal, which would have required fiduciaries in certain circumstances to vote or not to vote proxies, were removed from the final rule, as discussed above. Paragraph (e)(3)(iii) of the proposal expressly acknowledged the appropriateness of ERISA fiduciaries' adoption of proxy voting policies to help them more cost-effectively comply with their obligations under the proposal. Paragraph (e)(3)(iii) of the proposal provided for adoption of general proxy voting policies or procedures and provided three examples of policies that could be utilized by fiduciaries (sometimes referred to as ''permitted practices'') in paragraphs (e)(3)(iii)(A)–(C) of the proposal. The proposed permitted practices included conditions intended to require a fiduciary to make prudence-based judgments about the policies.

The Department received a number of general comments on paragraph (e)(3)(iii) of the proposal. Several commenters supported use of proxy voting policies to help fiduciaries reduce costs and compliance burdens, but suggested that the scope of relief for fiduciaries under paragraph (e)(3)(iii) of the proposal was unclear, noting that clear ''safe harbor'' relief was not afforded by the proposal. Commenters also asked about the extent to which fiduciaries following permitted practices would still be required to comply with particular provisions of the proposal that seemed more directed as evaluations of individual votes, *e.g.,* some of the recordkeeping provisions in the proposal. Commenters recommended that the permitted practices should be made clear safe harbors indicating that fiduciaries are deemed to satisfy their prudence and loyalty obligations under ERISA. Commenters argued that without such treatment the permitted practices would not offer effective options for easing compliance burdens and associated costs as intended by the Department. Commenters also requested confirmation that plan fiduciaries have flexibility to adopt proxy voting policies in addition to the specific examples described in the rule. Other commenters did not support paragraph (e)(3)(iii) of the proposal, asserting that the proposal would effectively compel ERISA plans to adopt one of the permitted practices by imposing the proposal's burdensome cost-benefit analysis requirements.

The Department has decided to retain, with modifications, the framework for adoption of proxy voting policies as set forth in paragraph (e)(3)(iii) of the proposal as paragraph (e)(3)(i) of the final rule. The provision in the final rule has been modified to more clearly provide safe harbor relief. The safe harbors apply to a fiduciary's duties of loyalty and prudence with respect to decisions on whether to vote, but do not apply to decisions on how to vote. Thus, a fiduciary will not breach its fiduciary responsibilities under sections 404(a)(1)(A) and 404(a)(1)(B) of ERISA with respect to decisions on whether to vote, provided such policies are developed in accordance with a fiduciary's obligations under ERISA as set forth in the applicable provisions of paragraphs (e)(2)(i) and (ii) of the final rule. Because the compliance burdens under the rule should be significantly reduced by other changes from the proposal described elsewhere (*e.g.,* the principles-based approaches and elimination of proposed paragraphs (e)(3)(i) and (ii)), the Department does not believe that fiduciaries will be compelled to adopt the proxy voting policies described in paragraph (e)(3)(i) of the final rule but rather will use them, as the Department intended, to provide cost-effective options for exercising shareholder rights in compliance with their fiduciary obligations under ERISA.

Thus, paragraph (e)(3)(i) of the final rule provides that in deciding whether to vote a proxy pursuant to paragraphs (e)(2)(i) and (ii) of the final rule, fiduciaries to plans may adopt proxy voting policies under which voting authority shall be exercised pursuant to specific parameters prudently designed to serve the plan's economic interest. The final rule further provides that paragraphs (e)(3)(i)(A) and (B) set forth optional means for satisfying the fiduciary responsibilities under section 404(a)(1)(B) of ERISA, provided such policies are developed in accordance with a fiduciary's prudence obligations under ERISA as set forth in the applicable provisions of paragraphs (e)(2)(i) and (ii) of the final rule. These safe harbors are intended to be applied flexibly rather than in a binary ''all or none'' manner, and may be used either independently or in conjunction with each other. The safe harbors are thus a means of establishing general proxy voting practices that allow plans to efficiently operationalize and manage shareholder rights consistent with the applicable fiduciary principles in paragraphs (e)(2)(i) and (ii). Paragraph (e)(3)(i) also makes clear that paragraphs (e)(3)(i)(A) and (B) are not intended to set forth an exclusive list of the policies that plans could adopt that would satisfy their responsibilities under the fiduciary principles in paragraphs (e)(2)(i) and (ii).

Paragraph (e)(3)(i)(A) sets forth the first of two safe harbor policies contained in the final rule. It describes a policy that voting resources will focus only on particular types of proposals that the fiduciary has prudently determined are substantially related to the issuer's business activities or are expected to have material effect on the value of the investment. The provision is substantively similar to the permitted practice described in paragraph (e)(3)(iii)(B) of the proposal. However, the proposed provision listed types of proposals that a fiduciary might prudently consider focusing voting resources on: Proposals relating to corporate events (mergers and acquisitions transactions, dissolutions, conversions, or consolidations), corporate repurchases of shares (buybacks), issuances of additional securities with dilutive effects on shareholders, or contested elections for directors. Commenters expressed concern that the Department did not provide any economic analysis for why matters listed in proposed paragraph (e)(3)(iii)(B) would be more material to shareholders than other issues, and argued that voting on a variety of issues not included in that list would be in the interest of ERISA plans. For example, a commenter pointed out that mutual fund proposals, which may present difficulties for these funds in achieving quorum as compared to solicitations made by corporate issuers, and votes to approve auditors were not included in the list but could be considered material to investors.

The list of matters included in the proposal was not intended as an exhaustive list of particular matters that merit consideration by fiduciaries. Nor was it intended to limit a fiduciary's flexibility to prudently consider other matters. The Department continues to believe that the listed issues are examples of matters that generally would be expected to have an economic impact on the value of the investment. Nonetheless, to avoid the potential for such a misperception, the Department is not including the list in paragraph (e)(3)(i)(A) of the final rule.

The final provision slightly revises the language used to describe the fiduciary's prudence determination to reflect a pecuniary-based analysis. The final rule also broadly references the value of the investment rather than the plan's investment to make it clear that the evaluation could be at the investment manager level dealing with a pool of investor's assets or at the individual plan level. Paragraph (e)(3)(i)(A) of the final rule thus describes a policy that voting resources will focus only on particular types of proposals the fiduciary has prudently determined are substantially related to the issuer's business activities or are expected to have a material effect on the value of the investment.[44]

Paragraph (e)(3)(i)(B) of the final rule sets forth the second safe harbor policy and is based on paragraph (e)(3)(iii)(C) of the proposal. The proposal provided that a fiduciary could adopt a policy of refraining from voting on proposals or particular types of proposals when the plan's holding of the issuer relative to the plan's total investment assets is below quantitative thresholds that the fiduciary prudently determines, considering its percentage ownership of the issuer and other relevant factors, is sufficiently small that the matter being voted upon is unlikely to have a material impact on the investment performance of the plan's portfolio (or investment performance of assets under management in the case of an investment manager). The proposal indicated that the Department was considering a specific quantitative upper limit for the threshold (*i.e.,* a cap) under paragraph (e)(3)(iii)(C), and solicited comments on setting this upper limit, including whether a maximum cap should be defined and, if so, what factors should be considered in setting a cap. In particular, the Department solicited comments on whether a five percent cap would be appropriate, or some other percent level of plan assets.

A commenter expressed the view that the permitted practice described in paragraph (e)(3)(iii)(C) to refrain from proxy voting would violate the requirement in ERISA section 404(a)(1)(B) that plan fiduciaries act ''with the care, skill, prudence, and diligence under the circumstances then prevailing [as] a prudent man acting in a like capacity and familiar with such matters.'' According to the commenter, the overwhelming majority of prudent experts—*i.e.,* the expert professionals who make up the investment management community—have determined that proxy voting is in their clients' interests. Another commenter disagreed with the Department's statement that voting shares of plan holdings that comprise a small portion of total plan assets rarely advances plans' economic interests. The commenter indicated that, depending on the size of a plan, even small relative positions can have a large dollar value.

Commenters also expressed concerns about potential negative unintended consequences of widespread adoption of the permitted practice. According to a commenter, if the majority of a plan's investments in portfolio companies fell within the parameters described in the permitted practice, this could leave the majority of the plan's portfolio un-voted, which in the aggregate would expose the plan investor to material risk even if the risk associated with each individual company was small. Additionally, according to commenters, non-voting by small plan investors could result in concentrating proxy votes in the hands of other investors whose interests might not align with the long-term interests of ERISA plans. Furthermore, non-voting by plans could result in companies with substantial portions of un-voted shares, and could also result in quorum requirements going unmet.

With respect to the Department's request for input on whether a percent cap would be appropriate, commenters generally opposed such a provision and suggested that the Department avoid specifying a percentage cap on the portion of the plan's portfolio that must be represented by an issuer for proxy votes to be considered.

The Department is not persuaded that the type of policy described in paragraph (e)(3)(iii)(C) of the proposal should be excluded from the final rule's safe harbor provision. The provision was designed to provide a fiduciary with flexibility to prudently tailor a quantitative threshold for a plan's portfolio, below which the outcome of the vote is unlikely to have a material impact on the performance of the plan's portfolio or, in situations where only a portion of the portfolio is being managed by an investment manager, the performance of the plan assets under

[44] The final rule uses the term ''material effect'' rather than ''significant impact.'' No substantive change is intended by the revision as the Department believes that ''significant impact'' is generally equivalent to ''material effect'' in this context. Use of the term materiality is intended to align the terminology consistent with the rest of the Investment Duties regulation. The Department believes that fiduciaries and investment managers are generally familiar with the concept of materiality from its use in connection with both ERISA and the Federal securities laws.

management. The Department believes that providing such an option in the final rule may be helpful to plans in reducing costs. The Department further believes that it can be prudent for a fiduciary to refrain from expending plan resources to vote on matters pertaining to a holding that makes up an immaterial portion because a fiduciary may prudently expect that voting on such matters will not have a material effect on performance. With respect to setting a cap, the Department does not believe it received sufficient information from comments to establish an upper limit in the final rule.

Paragraph (e)(3)(i)(B) of the final rule thus describes as the second safe harbor a policy of refraining from voting on proposals or particular types of proposals when holding in a single issuer relative to the plan's total investment assets, or the portion of a plan's assets being managed by an investment manager, is below a quantitative threshold that the fiduciary prudently determines, considering its percentage ownership of the issuer and other relevant factors, is sufficiently small that the matter being voted upon is not expected to have a material effect on the investment performance.[45] The final rule does not require a specific performance period for determining whether a material effect exists; fiduciaries must therefore prudently decide an appropriate performance period for use in its proxy voting policies under this safe harbor.

The Department notes that paragraph (e)(3)(iii)(A) of the proposal is not being incorporated in the final rule. Paragraph (e)(3)(iii)(A) of the proposal described a policy of voting proxies in accordance with the voting recommendations of a corporation's management on proposals or types of proposals that the fiduciary prudently determined would be 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 concerns a matter that may present heightened management conflicts of interest or is likely to have a significant economic impact on the value of the plan's investment. Commenters expressed the view that this permitted practice would be unprecedented, indicating that the Department has never previously indicated that a fiduciary may assume that another person is acting in the best interest of the plan. Rather, according to a commenter, the Department's consistent position is that a fiduciary must prudently select and monitor both fiduciary and non-fiduciary service providers. The commenter questioned this provision's consistency with other provisions of the proposal, noting that under other provisions of the proposal plan fiduciaries would be required to increase their due diligence on proxy advisory firms consistent with prudence and loyalty obligations, but this permitted practice would allow them to follow corporate directors in deciding what is in the best interest of the fiduciaries' plan participants without undertaking similar due diligence.

A commenter specifically noted that proxy advisory firms that are registered with the SEC under the Advisers Act owe their clients fiduciary duties of care and loyalty and suggested that if the permitted practice for management recommendations under paragraph (e)(3)(iii)(A) was adopted, then the Department should create a permitted practice for fiduciaries to rely on such firms. Commenters also questioned the safeguards offered by a permitted practice that relies on fiduciary duties that officers and directors owe to a corporation based on state corporate laws. A commenter stated that such a standard is lower that the fiduciary standard of care under ERISA. The commenter further stated that Delaware corporate law authorizes companies to waive director liability for breaches of the duty of care, and that corporate conflicts of interest with the company may also be waived upon approval of non-interested directors. Another commenter criticized reliance on fiduciary duties under state corporate law by noting that the law imposes these duties because management's interests can and do differ from those of the company's shareholders, and state corporate law requires shareholder votes precisely because managers' fiduciary duties alone are not adequate to align management's and shareholders' interests.

The Department notes that some of the commenters may have misread paragraph (e)(3)(iii)(A) as establishing unconditional blanket reliance on management recommendations. The proposal expressly limited reliance on management recommendations to proposals or types of proposals that the fiduciary had prudently determined would be unlikely to have a significant impact on the value of the plan's investment. Nonetheless, based on concerns expressed by commenters, and on the Department's separate decision to remove the requirement not to vote in certain situations, the Department decided to not adopt this permitted practice in the final rule's safe harbor provisions.

Commenters also provided several suggestions for additional permitted practices, none of which the Department has adopted. Several recommended a policy based on a determination that voting would not result in material additional costs to the plan. There is no need to include this permitted practice (or safe harbor) because the final rule does not have an express prohibition on voting based on the balance of economic effect and costs. Other commenters suggested permitted practices for following prudently designed and applied proxy voting guidelines. The Department does not believe it is necessary or appropriate to include such a safe harbor. Paragraph (e)(3)(i) already states that fiduciaries may adopt proxy voting policies providing that the authority to vote a proxy shall be exercised pursuant to specific parameters prudently designed to serve the plan's economic interest. Another commenter suggested that if the rule retains a permitted practice that permits a fiduciary to follow management recommendations, then the Department should add a permitted practice that permits following recommendations of the proxy advisory firm if the adviser owes a fiduciary duty to its clients. The Department has not retained the permitted practice regarding following management recommendations and believes that proxy advisory firms are adequately addressed in other provisions of the final rule.

Paragraph (e)(3)(ii) of the final rule relates to the review of proxy voting policies adopted under paragraph (e)(3)(i). The corresponding provision at paragraph (e)(3)(iv) of the proposal, applicable to the proposal's permitted practices, required plan fiduciaries to review any proxy voting policies adopted pursuant to paragraph (e)(3)(iii) of the proposal at least once every two years. The Department explained that the proposed requirement was appropriate to ensure a plan's proxy voting policies remain prudent given ongoing changes in financial markets and the investment world, but solicited comments on whether some other maximum interval for review would be appropriate.

Commenters suggested that a two-year requirement would be unnecessary and recommended removal. Commenters

[45] The proposal referred to ''the outcome of the vote,'' rather than ''the matter being voted upon.'' This final rule uses ''the matter being voted upon'' to make it clear that whether the fiduciary's voting power could sway the vote one way or the other is not relevant to application of the safe harbor. Rather, the point is that the plan's holding would be sufficiently small that any outcome of the vote (and any consequent changes to the value of the underlying asset) would have no material effect on the investment performance of the plan.

expressed the view that review of permitted practices should be based on facts and circumstances and left to the fiduciary to decide. A commenter also expressed concern that a specific review requirement in the rule could create potential liability for fiduciaries in their ongoing monitoring of other plan policies, such as investment policy statements, fiduciary charters, plan expenses and other policies, or in connection with the frequency of requests for proposals.

After considering comments, the Department has decided to remove the specific two-year requirement and provide a general requirement for periodic review of policies. The Department understands that general industry practice is to review investment policy statements approximately every two years and expects that fiduciaries will review proxy voting policies with roughly the same frequency. Nevertheless, the Department is persuaded that it is unnecessary to set an exact deadline and that doing so could create liability based on a technical temporal violation of the rule. As a result, paragraph (e)(3)(ii) of the final rule provides that plan fiduciaries shall periodically review proxy voting policies adopted pursuant to paragraph (e)(3)(i) of the final rule.

Paragraph (e)(3)(iii) of the final rule relates to the effect of proxy voting policies adopted under the final rule's safe harbor provision. It is based on paragraph (e)(3)(v) of the proposal, which provided that no policies adopted under paragraph (e)(3)(iii) of the proposal would have precluded, or imposed liability for, submitting a proxy vote when the fiduciary prudently determines that the matter being voted upon would have an economic impact on the plan after taking into account the costs involved, or for refraining from voting when the fiduciary prudently determines that the matter being voted upon would not have an economic impact on the plan after taking into account the costs involved.

A commenter indicated that paragraph (e)(3)(v) of the proposal was not sufficient to provide safe harbor relief for fiduciaries following permitted practices under the proposal. Another commenter expressed the view that the provision was not broad enough and should expressly permit fiduciaries to consider any prudent alternative courses of action for any particular proxy issue that may otherwise fall within the description of a permitted practice.

The Department believes that paragraph (e)(3)(i) of the final rule provides sufficient clarity with respect to the Department's intended safe harbor treatment of proxy voting policies adopted under paragraph (e)(3) of the final rule. The Department also believes that the principles-based approach in the final rule provides sufficient flexibility for fiduciaries to exercise prudent judgment in making proxy voting determinations. Changes have been made to paragraph (e)(3)(iii) of the final rule to reflect this principles-based approach.

Paragraph (e)(3)(iii) of the final rule provides that no proxy voting policies adopted pursuant to paragraph (e)(3)(i) of this section shall preclude, or impose liability for, submitting a proxy vote when the fiduciary prudently determines that the matter being voted upon is expected to have a material effect on the value of the investment or the investment performance of the plan's portfolio (or investment performance of assets under management in the case of an investment manager) after taking into account the costs involved, or refraining from voting when the fiduciary prudently determines that the matter being voted upon is not expected to have such a material effect after taking into account the costs involved. In light of the potentially large number of individual proxy votes that may need to be considered on an annual basis, the safe harbor provisions are intended to apply and operationalize the fiduciary principles described in the final rule for a particular plan in a cost-efficient manner and provide an alternative to retaining a proxy advisory firm to provide advice on each vote. Paragraph (e)(3)(iii) of the final rule shields a fiduciary from liability to the extent that the fiduciary deviates from policies adopted pursuant to the safe harbors based on the fiduciary's conclusion that a different approach in a particular case is in the economic interests of the plan considering the specific facts and circumstances.

(iv) Paragraph (e)(4)

Paragraphs (e)(4)(i) and (ii) of the final rule, like the proposal, reflect longstanding interpretive positions published in the Department's prior Interpretive Bulletins. Paragraph (e)(4)(i)(A) of the proposal stated that the responsibility for exercising shareholder rights lies exclusively with the plan trustee, except to the extent that either (*1*) the trustee is subject to the directions of a named fiduciary pursuant to ERISA section 403(a)(1), or (*2*) the power to manage, acquire, or dispose of the relevant assets has been delegated by a named fiduciary to one or more investment managers pursuant to ERISA section 403(a)(2). Paragraph (e)(4)(i)(B) of the proposal provided that where the authority to manage plan assets has been delegated to an investment manager pursuant to ERISA section 403(a)(2), the investment manager has exclusive authority to vote proxies or exercise other shareholder rights appurtenant to such plan assets, except to the extent the plan or trust document or investment management agreement expressly provides that the responsible named fiduciary has reserved to itself (or to another named fiduciary so authorized by the plan document) the right to direct a plan trustee regarding the exercise or management of some or all of such shareholder rights.

A commenter indicated that paragraph (e)(4)(i) of the proposal was unclear as to trustee responsibilities with respect to voting directed by plan participants pursuant to plan provisions. As discussed below, a new paragraph (e)(5) was added to the final rule to address ''pass-through'' or ''participant-directed'' voting. Paragraph (e)(4)(i)(A) in the final rule is unchanged from the proposal, with a correction of a typographical error. Paragraph (e)(4)(i)(B) in the final rule is unchanged from the proposal.

Paragraph (e)(4)(ii) of the proposal described obligations of an investment manager of a pooled investment vehicle that holds assets of more than one employee benefit plan. It stated that 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. It also provided that compliance with ERISA section 404(a)(1)(D) requires the 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 the Investment Duties regulation, 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 the Investment Duties regulation before deciding to retain the investment manager.

Commenters indicated that the proposal's requirement to reconcile conflicting policies of investing plans and engage in proportionate voting to reflect conflicting policies would be highly burdensome for investment managers. A commenter noted that it is sometimes not possible to instruct a single client's holding within the fund differently than other clients, as ''split-voting'' is not permitted practice in certain markets or custodian banks. Commenters also indicated that paragraph (e)(4)(ii) of the proposal did not reflect current industry standard practice that investment in a plan asset vehicle is generally conditioned on acceptance of the investment objectives, guidelines, and policies that apply to the vehicle. Some commenters recommended deletion of the proposed requirement to reconcile conflicting policies of ERISA plans. Other commenters suggested deleting paragraph (e)(4)(ii) of the proposal entirely.

Commenters requested that the language in paragraph (e)(4)(ii) of the proposal addressing a plan's acceptance of an investment manager's proxy voting policy be modified to clarify that the investment manager's investment policy statement or proxy voting policy must be consistent with Title I of ERISA, but are not required to be consistent with the proposed rule. Commenters indicated that investment managers would have difficulties performing the plan-specific evaluations required by the proposal. These issues are discussed more generally above. A commenter also indicated that even if the rule were to allow elimination of the plan-specific evaluation, the task to make changes to an investment manager's policies would still be enormous. According to the commenter, the trust's proxy voting guidelines would likely require revision, and once revised, would need to be presented, explained, and accepted by each participating plan, including non-ERISA plans not subject to the rule. Similarly another commenter suggested that the subtle differences between paragraph (e)(4)(ii) of the proposal and the analogous provision in IB 2016–01 might cause an investment manager, in order to protect all of its clients, to adopt a revised investment policy statement that it would require participating plans to accept, and that the process would involve both drafting that policy and obtaining consent from investing plans.

The Department is not persuaded to remove paragraph (e)(4)(ii) from the final rule or change the language regarding reconciliation of conflicting policies of investing plans or proportionate voting. Similar guidance has been consistently part of the Department's prior Interpretive Bulletins in this area. As to the requirement that policies must be consistent with Title I of ERISA and the final rule and difficulties associated with plan specific evaluations, the Department believes that changes in paragraph (e)(2)(i) and (ii) of the final rule should address commenters' concerns. With respect to the commenter's identification of subtle differences between paragraph (e)(4)(ii) of the proposal and the relevant portion of IB 2016–01, the Department acknowledges that the language is not identical.[46] However, the Department did not intend the language changes to fundamentally alter that guidance. Like IB 2016–01, paragraph (e)(4)(ii) recognizes that there may be circumstances under which an investment manager of a pooled investment vehicle that holds assets of more than one plan may be subject to conflicting policies of investing plans, but that the manager may avoid conflicting policies by requiring investors to accept the investment manager's policies before they are allowed to invest.[47] However, paragraph (e)(4)(ii) adds language that describes the associated obligations of plan fiduciaries in making the decision to accept the investment manager's policies. Commenters did not question whether an ERISA fiduciary should assess an investment manager's investment policy statement for consistency with ERISA prior to accepting it. To the extent that the commenter's concerns about differences from the relevant portion of IB 2016–01 relate to the requirement that the manager's policies must be consistent with the final rule, the Department believes changes in paragraph (e)(2)(i) of the final rule, as described above, should address this concern. As a result, paragraph (e)(4)(ii) of the final rule is being adopted substantially as proposed.

(v) Paragraph (e)(5)

A number of commenters indicated that the proposal did not specifically address proxy rights passed through to plan participants. A commenter explained that participants may invest in publicly-traded companies, as well as mutual funds and other securities, through a self-directed brokerage window offered by their plans. According to the commenter, self-directed brokerage windows involve the broker passing voting rights through to the participants. Further, participant-directed plans, such as those structured to meet ERISA section 404(c) and related regulations, sometimes allow participants to invest in company stock and pass through voting to them. According to the commenter, many ERISA-covered plans have been drafted to explicitly provide that plan participants are deemed to be ''named fiduciaries'' when they vote securities held by their plan accounts. Commenters argued that the structure and provisions of the proposed regulation did not account for such ''pass-through'' or ''participant-directed'' voting activity, and requested that the Department expressly exclude such voting activity from the rule or provide clarification as to application of the proposed rule's requirements in the context of pass-through of voting rights, including the responsibilities of trustees in connection with the actual votes of participants and whether participants when exercising their proxy voting rights would be treated as fiduciaries under the rule.

The Department agrees that the proposal was not intended to address

[46] Specifically, IB 2016–01 stated: ''An investment manager of a pooled investment vehicle that holds assets of more than one employee benefit plan may be subject to a proxy voting policy of one plan that conflicts with the proxy voting policy of another plan. Compliance with ERISA section 404(a)(1)(D) would require the 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)) and, if necessary and to the extent permitted by applicable law, vote the relevant proxies to reflect such policies in proportion to each plan's interest in the pooled investment vehicle. If, however, the investment manager determines that compliance with conflicting voting policies would violate ERISA section 404(a)(1)(D) in a particular instance, for example, by being imprudent or not solely in the interest of plan participants, the investment manager would be required to ignore the voting policy that would violate ERISA section 404(a)(1)(D) in that instance. Such an investment manager may, however, require participating investors to accept the investment manager's own investment policy statement, including any statement of proxy voting policy, before they are allowed to invest. As with investment policies originating from named fiduciaries, a policy initiated by an investment manager and adopted by the participating plans would be regarded as an instrument governing the participating plans, and the investment manager's compliance with such a policy would be governed by ERISA section 404(a)(1)(D).''

[47] *See* 59 FR 38860, 38863 (July 29, 1994) (''Nothing in ERISA, however, prevents such an investment manager from maintaining a single investment policy, including a proxy voting policy, and requiring all participating investors to give their asse[n]t to such policy as a condition of investing.'').

the sort of pass-through voting that the commenters described. Accordingly, the final rule includes an express provision in new paragraph (e)(5) stating that the final rule does not apply to voting, tender, and similar rights with respect to such securities that are passed through pursuant to the terms of an individual account plan to participants and beneficiaries with accounts holding such securities. That should not be read as an indication that plan trustees and other plan fiduciaries do not have fiduciary obligations with respect to such practices. Prior Department guidance recognized that in certain circumstances a trustee may follow the instructions of participants in an eligible individual account plan that expressly states that a trustee is subject to the direction of plan participants with respect to certain decisions regarding the management of their account. In such a case, under section 403(a)(1) of ERISA, the trustee must follow the direction of participants if those directions are proper, made in accordance with plan terms, and not contrary to ERISA.[48] Plan trustees and other fiduciaries would continue to have to comply with ERISA's prudence and loyalty provisions with respect to the pass through of votes to plan participants and beneficiaries, and can continue to rely on the Department's prior guidance with respect to such participant-directed voting, including 29 CFR 2550.404c-1 implementing ERISA section 404(c)(1) to participant-directed pass through voting.

(vi) Paragraphs (g) and (h)

Paragraph (g) provides the applicability dates for the final rule. Under paragraph (g), the final rule will be applicable thirty days after the date this final rule is published in the **Federal Register**.[49] One commenter requested clarity with respect to whether the proposed applicability date applied only to paragraph (e) or to the entirety of § 2550.404a–1. Paragraphs (g)(1) and (g)(3) of the final rule state that the applicability date for paragraph (e) is thirty days after the date this final rule is published in the **Federal Register** and shall apply to exercises of shareholder rights after such date. A number of commenters on the proposal stated that the proposed 30-day effective date period would not accommodate the essential and lengthy transition processes that would be necessary for plan fiduciaries to fully comply with the rule.[50] These commenters requested extensions up to 12 or 18 months after publication of a final rule. Alternatively, or in addition to extending the applicability date, commenters requested that if the Department retains the 30-day provision, that the final rule include guidance that would permit affected parties a more reasonable amount of time to comply with the rule. Commenters proffered a variety of suggestions that would help plan fiduciaries and others manage this new process, including a different applicability date, a transition rule, a grandfather rule for existing voting arrangements, and a temporary non-enforcement policy.

The Department is not extending the applicability date, particularly given the benefits this final rule affords to participants and beneficiaries. Furthermore, the Department believes that the final rule does not represent so significant a change from existing guidance that fiduciaries can reasonably claim impossibility in timely implementing most of its requirements. However, the Department agrees that for certain portions of the final rule, a later applicability date will address concerns of some commenters with respect to their ability to comply with the rule within the 30-day effective period. Paragraph (g)(3) grants fiduciaries until January 31, 2022, to comply with the requirements of paragraphs (e)(2)(ii)(D) and (E), (e)(2)(iv), and (e)(4)(ii) of the final rule. This delay gives fiduciaries additional time in making any modifications with respect to their use of proxy advisory firms and other service providers and for reviewing any proxy voting policies of pooled investment vehicles by investment managers. However, fiduciaries that are investment advisers registered with the SEC must comply with the 30-day effective date with respect to paragraphs (e)(2)(ii)(D) and (E) as such provisions are intended to be aligned with existing obligations under the Advisers Act, including Rules 204–2 and 206(4)-6 thereunder and the 2019 SEC Guidance and 2020 SEC Supplemental Guidance.[51]

Finally, paragraph (h) of the final rule, as proposed, continues to provide that should a court of competent jurisdiction hold any provision of the rule invalid, such action will not affect any other provision. Including a severability clause describes the Department's intent that any legal infirmity found with part of the final rule should not affect any other part of the rule. The exact same paragraph is included in the final rule on Financial Factors in Selecting Plan Investments.

4. Interpretive Bulletin 2016–01 (IB 2016–01) and Field Assistance Bulletin 2018–01 (FAB 2018–01)

The final rule also withdraws IB 2016–01 and removes it from the Code of Federal Regulations. Accordingly, as of publication of the final rule, IB 2016–01 may no longer be relied upon as reflecting the Department's interpretation of the application of ERISA's fiduciary responsibility provisions to the exercise of shareholder rights and written statements of investment policy, including proxy voting policies or guidelines.

FAB 2018–01 concerned both ''ESG Investment Considerations'' and ''Shareholder Engagement Activities.'' The portion of FAB 2018–01 under the heading of ''ESG Investment Considerations'' was superseded by the Department's final rule on ''Financial Factors in Selecting Plan Investments.''[52] Similarly, the portion of FAB 2018–01 under the heading ''Shareholder Engagement Activities'' will be superseded by this final rule and this accompanying preamble. Since that discussion is the sole remaining substantive portion of FAB 2018–01, as of the effective date of the final rule, FAB 2018–01 will no longer be considered current guidance issued by the Department.

C. Miscellaneous Issues

Constitutional Issues

A number of commenters raised concerns that the proposal, or specific provisions of the proposal, may be inconsistent with certain rights afforded shareholders by the First and Fifth Amendments in the Constitution's Bill of Rights. The Department disagrees

[48] *See* Letter from Deputy Assistant Secretary Lebowitz to Thobin Elrod (Feb. 23, 1989); Letter from Assistant Secretary Berg to Ian Lanoff (Sept. 28, 1995).

[49] One commenter argued that the rule is a ''major rule'' under the Congressional Review Act and thus may not be effective earlier than 60 days after publication in the **Federal Register**. As discussed in the Regulatory Impact Analysis below, the Office of Management and Budget has determined this rule is not a ''major rule'' for Congressional Review Act purposes and is therefore not subject to the delayed 60-day effective date.

[50] Commenters pointed out that plan sponsors and other fiduciaries would need to review, amend, and possibly renegotiate existing contracts with investment managers, proxy advisory firms, and other service and investment providers. Some commenters also expressed more specific concerns, for example, that, with respect to pooled investment vehicles, it may be necessary to obtain approval of revised investment policy statements from participating plans, which would be difficult to obtain in only 30 days.

[51] The final rule includes a technical language change in paragraph (g) to conform paragraph (g) to **Federal Register** drafting conventions regarding the use of ''effective date'' versus ''applicability date'' terminology.

[52] 85 FR at 72872.

with these constitutional arguments and, further, believes that the lack of merit of those arguments is even more pronounced in light of modifications to the proposed rule adopted in the final rule. Rather, the final rule is designed to help these ERISA fiduciaries meet statutory standards, in particular the requirement that ERISA fiduciaries must carry out their duties relating to the exercise of shareholder rights prudently and solely for the economic benefit of plan participants and beneficiaries. The Department's view of the scope of factors to be considered by an ERISA fiduciary when managing plans assets was articulated as recently as 2014 by the Supreme Court in *Fifth Third Bancorp* v. *Dudenhoeffer,* 573 U.S. 409, 421 (2014) (the ''benefits'' to be pursued by ERISA fiduciaries as their ''exclusive purpose'' do not include ''nonpecuniary benefits'').

First Amendment Free Speech and Exercise of Religion

Some commenters asserted that the proposal may violate the First Amendment's protection of free speech. The decision to vote shares or engage in shareholder activism is, they argued, a form of speech, and they claimed that the Department established strict conditions and costly burdens on the established mechanism by which shareholders (and therefore their representatives) are able to communicate their interests and provide for companies to take (or refrain from taking) certain actions. They also argued that the proposal was targeted at preventing support of ESG-related initiatives and, by increasing the costs associated with determining whether it is acceptable to vote, would force fiduciaries to use a permitted practice either to not support those initiatives or to vote with corporate management; thus, the commenters concluded that the proposal was both a content- and viewpoint-based restriction. The proposal, according to these commenters, could mandate that assets are managed in a manner that is inconsistent with the values and interests of ERISA investors. Similarly, a few commenters claimed that the proposal also may violate the First Amendment's protections for freedom of religion, because it would curtail the rights of religious organizations to vote in accordance with their beliefs.

The First Amendment bars the government from abridging freedom of speech or the right to assemble peaceably and from prohibiting the free exercise of religion.[53] The right of free speech protects the open expression of ideas without fear of government reprisal. Some commenters stated that the right to vote a proxy consistent with the participants' and beneficiaries' values is protected speech, and argued that the proposed rule's requirements would unconstitutionally limit this right.

These commenters relied predominantly on the premise that the proposal effectively would force fiduciaries either to not vote or to vote with management. As one commenter argued, the proposal would ''impose unique and burdensome restrictions on shareholder activities that may be contrary to the interests of a favored group, while removing those restrictions when the expressive activity favors the preferred group.'' However, the Department in this final rule has removed the provisions that these commenters argued would create a *fait accompli,* allegedly stifling fiduciaries' speech-through-proxy-vote. Because of those changes, these arguments are moot.

To the extent commenters would still argue that the final rule might run afoul of the Free Speech Clause, this argument is overbroad and inconsistent with Supreme Court precedent. ERISA requires fiduciaries to manage plan assets for the ''exclusive purpose'' of providing benefits and defraying expenses. Even if voting by a shareholder speaking for herself could be speech, as some commenters argued, proxy voting by a plan, which holds its shares in trust for its participants and beneficiaries, should appropriately and correctly be considered conduct. Consistent with *Dudenhoeffer,* fiduciary plan asset management activity must focus exclusively on providing ''benefits.'' That term refers to *financial* benefits (such as retirement income), and not to non-pecuniary goals. The final rule's provisions require that any proxy decision serves those financial benefits of participants and beneficiaries, a duty derived directly from the ERISA statute.

To the extent proxy voting by a plan is speech, ERISA's requirements and the final rule's standards of diligence and consideration of cost plainly satisfy the independent scrutiny that is required for regulations of commercial speech.[54] Moreover, the final rule is content- and viewpoint-neutral. The final rule does not require fiduciaries to say (or refrain from saying) anything in particular or take (or refrain from taking) any particular position, nor does it require fiduciaries to take action only on certain topics. The final rule instead requires that fiduciaries exercise authority over their proxies with the same loyalty and prudence applicable to all other aspects of their management of plan assets. And any restriction to express beliefs imposed by the rule still leaves open ample alternative channels to freely express those same beliefs.[55]

The Department also does not agree that the final rule violates the First Amendment's Free Exercise clause. The final rule is a neutral rule of general applicability and does not target any religious view.[56] The final rule's provisions aim solely to ensure that fiduciaries base proxy decisions of any kind exclusively on the financial benefits of participants and beneficiaries, as required by ERISA.[57] The impact on religion, if any, would be incidental and not violate the First Amendment.[58] Moreover, pursuant to ERISA section 4(b)(2), church plans, as defined in ERISA section 3(33), are not subject to ERISA and this regulation.[59]

Fifth Amendment Takings

A few commenters raised a different Constitutional concern—that the proposal may violate the Fifth Amendment's ''takings'' clause. Characterizing the right to vote a proxy as a plan asset, these commenters argue that the proposed rule would require ERISA plans to use their votes in a specific way, or relinquish them. The proposed rule's requirements, the commenters posited, are so burdensome as to prevent fiduciaries from fully exercising their voting rights.

The Department disagrees that the provisions of the final rule violate the Takings Clause. The Fifth Amendment prohibits the government from taking

[53] U.S. Const., amend. I.

[54] *See Cent. Hudson Gas & Elec. Corp.* v. *Pub. Serv. Comm'n of New York,* 447 U.S. 557, 564 (1980). Commenters generally argued that *Central Hudson's* commercial speech test would apply.

[55] *Clark* v. *Community for Creative NonViolence,* 468 U.S. 288, 293 (1984).

[56] *Church of the Lukumi Babalu Aye* v. *City of Hialeah,* 508 U.S. 520, 531 (1993) (''In addressing the constitutional protection for free exercise of religion, our cases establish the general proposition that [a law that is neutral and of general applicability need not be justified by a compelling governmental interest even if the law has the incidental effect of burdening a particular religious practice.], *Employment Div., Dept. of Human Resources of Ore.* v. *Smith,* 495 U.S. 872 (1990)'').

[57] *Fraternal Order of Police of Newark* v. *City of Newark,* 170 F.3d 359, 360 (3d Cir. 1999) (''Because the Department makes exemptions from its policy for secular reasons and has not offered any substantial justification for refusing to provide similar treatment for officers who are required to wear beards for religious reasons, we conclude that the Department's policy violates the First Amendment'').

[58] *See Fraternal Order of Police of Newark,* 170 F.3d at 360; *Smith,* 495 U.S. at 878–79.

[59] *See* 29 U.S.C. 1002(33).

private property for public use without just compensation.[60] A ''regulatory taking'' is one in which a government regulation is ''so onerous that its effect is tantamount to a direct appropriation or ouster.'' [61] The Government action must (1) affect a property interest and (2) go ''too far'' in so doing (*i.e.,* amount to a deprivation of all or most economic use or a permanent physical invasion of property).[62] How far is too far depends upon several factors, including ''the character of the governmental action, its economic impact, and its interference with reasonable investment-backed expectations.'' [63]

At the outset, the Takings Clause applies only when ''property'' is ''taken.'' The Department has stated that the act of voting proxy shares is a fiduciary act of managing plan assets.[64] The Department is not aware of any judicial authority that has addressed whether a shareholder right appurtenant to a share of stock, as opposed to the share of stock itself, is ''property'' for purposes of the Takings Clause and whether the ''taking'' analysis would involve an evaluation of the regulation's impact on the overall value of the stock. Nonetheless, even if the right to vote a proxy itself constitutes a constitutionally-protected property interest, neither the proposal nor this final rule ''takes'' that right or the underlying shares. Instead, the rule fully preserves the right to vote proxies in the economic interests of the plan. It is designed to protect, not diminish, participants' and beneficiaries' interests in their retirement benefits and the plan's economic interests by ensuring proxy votes do not subordinate those interests to non-pecuniary factors. The fiduciary maintains discretion to vote or not vote consistent with these interests. Given the Department's longstanding position that the plan's pecuniary interests guide the exercise of shareholder rights, there is no reasonable expectation that plans can make proxy voting decisions based on anything but plans' pecuniary interests.[65] Further, both plans and securities are already subject to extensive regulation under state and federal law.[66] Finally, the rule does not ''take'' property for public use, such as for public safety or historical preservation, but instead places parameters around proxy voting conduct that would fall outside of the prudence and loyalty duties found in the ERISA statute itself.

Administrative Procedure Act

A few commenters suggested that the Department's proposal was arbitrary and capricious and, more specifically, failed to comply with the Administrative Procedure Act. Also, although not necessarily framed in terms of the Department's compliance with the Administrative Procedure Act, a number of commenters asserted that the Department lacked sufficient evidentiary support for proposing the rule. For example, commenters pointed out that the Department suggested an increase in shareholder proposals as justification for the rule, which they argued is not relevant to whether fiduciaries are confused about their fiduciary obligations with respect to proxy voting, and that the Department did not cite to any enforcement action or other evidence that ERISA plan participants have been harmed or that ERISA plan fiduciaries are actually confused about their responsibilities. Other commenters disagreed and believed that the Department established sufficient evidence to support its proposal—for example, evidence that politically charged shareholder proposals result in the incursion of sometimes significant costs but do not demonstrably enhance shareholder value—and that the Department, therefore, is correct to limit voting on such proposals. Commenters supporting the rule also discussed evidence that proxy advisory firms, which exert massive amounts of influence over public companies, have well-documented deficiencies, including conflicts of interest, errors, and a lack of transparency.

Some commenters also argued that the proposal was a significant departure from prior Departmental guidance on shareholder rights without sufficiently establishing the existence of a problem to be solved, or otherwise providing a reason why the rule otherwise is necessary. Commenters also argued that no further clarification of the existing Interpretive Bulletin and Field Assistance Bulletin regarding fiduciaries' ERISA obligations with respect to proxy voting is necessary.

With respect to the arguments of commenters concerning the Administrative Procedure Act, the Department believes that there are sufficient reasons to justify the promulgation of this final rule, including the lack of precision and consistency in the marketplace with respect to ERISA fiduciary obligations with respect to exercises of shareholder rights, shortcomings in the rigor of the prudence and loyalty analysis by some fiduciaries and other market participants, and perceived variation in some aspects of the Department's past guidance. Further, the iterative Interpretive Bulletins since 1994, followed by the Field Assistance Bulletin issued in 2018, and the number of advisory opinions and information letters historically issued on this topic demonstrate the need for notice and comment guidance issued under the Administrative Procedure Act.[67] The Department does not believe that there needs to be specific evidence of fiduciary misbehavior or demonstrated injury to plans and plan participants in order to issue a regulation addressing the application of ERISA's fiduciary duties to the exercise of shareholder rights, including proxy voting, the use of written proxy voting policies and guidelines, and the selection and monitoring of proxy advisory firms.

The need for this regulation was also demonstrated by the disagreements among commenters on fundamental aspects of the proposal, which itself confirmed that a lack of clarity in fact exists and that ERISA fiduciaries and other market stakeholders would benefit from the Department's guidance in this final rule, as well as the confusion regarding the scope of fiduciaries' duties with respect to proxy voting and shareholder rights evidenced by the number of statements by stakeholders and others expressing a belief that fiduciaries are required by ERISA to always vote proxies. Moreover, under the Department's authority to administer ERISA, the Department may promulgate rules that are preemptive in nature and is not required to wait for widespread harm to occur. The Department can take steps to ensure that plans and plan participants and beneficiaries are protected prospectively and has the ability to issue regulations

[60] U.S. Const. amend. V.

[61] *Lingle* v. *Chevron U.S.A. Inc.,* 544 U.S. 528, 537 (2005).

[62] *Ruckelshaus* v. *Monsanto Co.,* 467 U.S. 986, 1000–01, 1005 (1984).

[63] *Id.* at 1005 (quoting *PruneYard Shopping Ctr.* v. *Robins,* 447 U.S. 74, 832 (1980)).

[64] *Avon Letter, supra* note 6.

[65] *Penn Central Transp. Co.* v. *City of New York,* 438 U.S. 104, 127 (1978) (finding historical preservation law not a taking in part because it permitted owner to obtain a reasonable return on its investment.).

[66] *See, e.g., Ruckelshaus,* 467 U.S. at 1007 (1984) (noting that expectations are necessarily adjusted in areas that ''ha[ve] long been the source of public concern and the subject of government regulation''); *Franklin Mem'l Hosp.* v. *Harvey,* 575 F.3d 121, 128 (1st Cir. 2009) (holding that a claimant's investment-backed expectations were ''tempered by the fact that it operate[d] in the highly regulated hospital industry'').

[67] *See* Executive Order 13891, 84 FR 55235 (Oct. 15, 2019), promoting notice-and-comment rulemaking for guidance.

to ensure that fiduciaries follow their statutory duties and mitigate the possibility of future violations.

The Department also believes that proceeding through notice-and-comment rulemaking rather than promulgating further interpretive guidance has other benefits, including the benefit of public input and the greater stability of codified rules. Proceeding in this manner is also consistent with the principles of Executive Order 13891 and the Department's recently issued PRO Good Guidance rule, which emphasize the importance of public participation, fair notice, and compliance with the Administrative Procedure Act.

Tension With State Corporate Law

Some commenters argued that the proposal, if finalized, would undermine state corporate laws, which reflect the inherent value of shareholder voting, threaten good corporate governance, and impede shareholders' voting rights. The Department is, according to these commenters, overstepping its authority and substituting its opinion for that of shareholders, the owners of corporations, as to what is important for corporate management and business affairs. Shareholders' exercise of voting rights is a critical ''check'' on the principal-agent conflict that arises from the separation of ownership and management in modern corporate law. Other commenters asserted that, in addition to potentially conflicting with corporate law, the Department's rule may conflict with corporations' and institutional investors' existing policies for shareholder voting, policies that have evolved over time, in response to real economic and financial developments, to enhance the efficiency and efficacy of the shareholder voting process.

The Department disagrees with commenters that this rulemaking creates any real conflict with state corporate laws. Although the rule will affect ERISA plan fiduciaries as to whether and how they exercise certain shareholder rights, the rule will not impact such rights themselves. Commenters failed to provide specific examples demonstrating any material conflict or compliance issue concerning these state laws.

Coordination With Other Federal Laws and Policies

Some commenters expressed their concern that the rule, if finalized, could negatively impact the U.S. securities markets to the extent the rule interferes with other federal agencies' objectives—for example, by making it more difficult for the SEC to perform its mission of protecting securities markets and investors. According to commenters, in efficient markets shareholders are assumed to exercise their voting rights to ensure that investments are managed in their best interests, and the proposed rule would frustrate evolving market efficiencies concerning when and how shareholders vote proxies. Commenters also alleged that potential conflicts could arise for financial market stakeholders who are subject to the laws of other federal agencies, including the SEC, the Office of the Comptroller of the Currency, and the Commodity Futures Trading Commission.

The Department believes that the changes made to the final rule mitigate any concerns with respect to potential conflicts with other regulatory regimes. For example, the final rule is intended to align with comparable SEC requirements imposed on investment advisers with respect to recordkeeping.[68] Both the proposed and final rules were sent to the SEC and other federal agencies as part of the inter-agency review conducted by the Office of Management and Budget pursuant to Executive Order 12866. Also, the final rule, as described above, adopts a principles-based approach that is fundamentally consistent with the Department's published interpretive guidance in this area beginning in 1994. Accordingly, the Department does not agree that the final rule will make it more difficult for the SEC or any other federal agency to perform their missions or that the final rule will have any negative impact on the U.S. securities markets. Rather, many public comments welcomed the final rule as appropriately describing the prudence and loyalty obligations of ERISA fiduciaries in connection with the exercise of shareholder rights.

Consistency With International Practices and Regulatory Trends

A few commenters also raised concerns about how the proposal, if finalized, would impact international investment. For example, one commenter, a financial services provider, claimed that the rule's mandate that proxy voting be based solely on an ERISA plan's economic interests is inconsistent with the provider's clients' expectations, and also with investment stewardship standards outside of the United States. The commenter claimed that asset managers in the European Union and other developed nations are increasingly subject to standards exactly opposite to those proposed by the Department, which incorporate (and sometimes require) consideration of ESG factors. Further, some international securities issuers require that investors vote proxies, and commenters queried what a plan fiduciary should do in such cases.

This final rule reflects ERISA's requirements. Fiduciaries of ERISA-covered pension and other benefit plans are statutorily bound to manage those plans, including shareholder rights appurtenant to shares of stock, with a singular goal of maximizing the funds available to pay benefits under the plan. The duties of prudence and loyalty under ERISA may not be the same investment standards the commenters referenced under which international regulation of proxy voting and other exercises of shareholder rights is taking place. Accordingly, international trends or the actions of regulators in other countries are not an appropriate gauge for evaluating ERISA's requirements as they apply to fiduciary management of investments, including the topics covered by this final rule relating to the exercise of shareholder rights, including proxy voting, the use of written proxy voting policies and guidelines, and the selection and monitoring of proxy advisory firms. Moreover, to the extent foreign legal and financial standards condone sacrificing returns to consider non-pecuniary objectives, they are inconsistent with the fiduciary obligations imposed by ERISA.

As to commenters' assertion that some international securities issuers require that investors vote proxies, as discussed above, the final rule does not carry forward the provision from the proposal stating that 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 after considering those factors described in paragraph (e)(2)(ii) of the proposed rule, taking into account the costs involved (including the cost of research, if necessary, to determine how to vote). The Department also believes that such a voting requirement by an issuer of securities held by a plan would be a relevant consideration for the plan fiduciary when applying the more principles-based approach adopted in the final rule when deciding whether to vote. However, the Department has previously noted that in deciding

[68] In pursuing its consultations with other regulators, the Department aimed to avoid conflict with other federal laws and minimize duplicative provisions between ERISA and federal securities laws. However, the governing statutes do not permit the Department to make obligations under ERISA identical in all respects to duties under federal securities laws.

whether to purchase shares that may involve out-of-the-ordinary costs or unusual requirements—specifically referencing as an example voting proxies on shares of certain foreign corporations—the responsible fiduciary should consider whether the difficulty and expense of voting the shares is reflected in the market price.[69] Similarly, in the Department's view, in deciding whether to purchase or retain shares, a fiduciary would have to consider proxy voting requirements of an issuer that conflict with the fiduciary's duties of prudence and loyalty under ERISA or that interfere with the fiduciary's ability to comply with those duties.

D. Regulatory Impact Analysis

This section analyzes the regulatory impact of the Department's final regulation amendments to the ''Investment Duties'' regulation in 29 CFR 2550.404a–1 addressing the application of the prudence and exclusive purpose responsibilities under ERISA with respect to the exercise of shareholder rights, including proxy voting, the use of written proxy voting policies and guidelines, and the selection and monitoring of proxy advisory firms. As stated earlier in this preamble, in connection with proxy voting, the Department's longstanding position articulated in sub-regulatory guidance that was first issued in the 1980s is that the fiduciary act of managing plan assets includes the management of voting rights (as well as other shareholder rights) appurtenant to shares of stock. In carrying out these duties, ERISA mandates that fiduciaries act ''prudently'' as well as ''solely in the interest'' and ''for the exclusive purpose'' of providing benefits to participants and their beneficiaries.[70]

This regulatory project was initiated because the Department believes there is a persistent misunderstanding among some fiduciaries and other stakeholders with respect to ERISA's requirements regarding proxy voting and the exercise of shareholder rights. This misunderstanding may be due in part to varied statements the Department has made on the consideration of non-pecuniary or non-financial factors in sub-regulatory guidance about those activities. This final rule provides certainty to plan administrators and benefits ERISA plan participants by eliminating the misunderstanding that exists among some stakeholders that ERISA fiduciaries are required to vote all proxies rather than only proxies determined to have a net positive economic impact on the plan. The final rule also supplements the Department's sub-regulatory guidance by specifying actions fiduciaries can take to ensure they are meeting their long-standing obligation under ERISA to act prudently, solely in the interests of participants and beneficiaries, and for the exclusive purpose of providing benefits and defraying reasonable plan expenses.

While the Department expects that this final rule will benefit plans and participants overall, it also will impose some compliance costs to the extent that fiduciaries do not currently meet specific requirements found in the final rule. However, as discussed in the cost section below, the Department has made significant modifications to the proposal in the final rule by taking a less prescriptive, principles-based approach to the subject matter that focuses on whether a fiduciary has a prudent process for voting and other exercises of shareholder rights. These changes will significantly reduce the potential compliance costs for fiduciaries.

The benefits, costs, and transfer impacts associated with the final rule depend on the number of plan fiduciaries that are currently not following or misinterpreting the Department's existing sub-regulatory guidance. While the Department does not have sufficient data to estimate the number of such fiduciaries, the Department expects the number is small because the Department believes that most fiduciaries largely comply with the Department's existing sub-regulatory guidance in this area, which is consistent with the principles-based requirements of the final rule. The Department expects that the benefits of the rule will be appreciable for participants and beneficiaries covered by plans with noncompliant investment fiduciaries. If the Department's assumption regarding the number of noncompliant fiduciaries is understated, the proposed rule's benefits, costs, and transfer impacts will be proportionately higher; however, even in this instance, the Department believes that the final rule's benefits still justify its costs.

1. Relevant Executive Orders

The Department has examined the effects of this rule as required by Executive Order 12866,[71] Executive Order 13563,[72] Executive Order 13771,[73] the Congressional Review Act,[74] the Paperwork Reduction Act of 1995,[75] the Regulatory Flexibility Act,[76] Section 202 of the Unfunded Mandates Reform Act of 1995,[77] and Executive Order 13132.[78]

Executive Orders 12866 and 13563 direct agencies to assess the costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects; distributive impacts; and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility.

Under Executive Order 12866, ''significant'' regulatory actions are subject to review by the Office of Management and Budget (OMB). Section 3(f) of the Executive order defines a ''significant regulatory action'' as an action that is likely to result in a rule (1) having an annual effect on the economy of $100 million or more in any one year, or adversely and materially affecting a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or state, local or tribal governments or communities (also referred to as ''economically significant''); (2) creating a serious inconsistency or otherwise interfering with an action taken or planned by another agency; (3) materially altering the budgetary impacts of entitlement grants, user fees, or loan programs or the rights and obligations of recipients thereof; or (4) raising novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in the Executive order.

OMB has determined that this rule is not economically significant within the meaning of section 3(f)(1) of the Executive Order 12866, but that it is significant within the meaning of section 3(f)(4) of the Executive order. Therefore, the Department provides an assessment of the potential costs, benefits, and transfers associated with

[69] *See, e.g.,* 29 CFR 2509.2016–01 (last paragraph in the section entitled ''Proxy Voting'').

[70] ERISA section 404(a)(1). *See also* ERISA section 403(c)(1) (''[T]he assets of a plan shall never inure to the benefit of any employer and shall be held for the exclusive purposes of providing benefits to participants in the plan and their beneficiaries'').

[71] Regulatory Planning and Review, 58 FR 51735 (Oct. 4, 1993).

[72] Improving Regulation and Regulatory Review, 76 FR 3821 (Jan. 18, 2011).

[73] Reducing Regulation and Controlling Regulatory Costs, 82 FR 9339 (Jan. 30, 2017).

[74] 5 U.S.C. 804(2) (1996).

[75] 44 U.S.C. 3506(c)(2)(A) (1995).

[76] 5 U.S.C. 601 *et seq.* (1980).

[77] 2 U.S.C. 1501 *et seq.* (1995).

[78] Federalism, 64 FR 43255 (Aug. 10, 1999).

this final rule below. OMB has reviewed the final rule pursuant to the Executive order. Pursuant to the Congressional Review Act, OMB has determined that this final rule is not a ''major rule,'' as defined by 5 U.S.C. 804(2).

1. Introduction

ERISA plan assets comprise a substantial stake of the shares of public companies. In 2018, pension plan assets contained stock holdings of $1.7 trillion; such holdings made up 27 percent of large defined benefit plan assets and 25 percent of large defined contribution plan assets.[79] However, ERISA pension holdings represent a decreasing share of all corporate equity. ERISA defined benefit and defined contribution plans held just 5.5 percent of total corporate equity in 2019, down from a high of 22 percent in 1985.[80]

Prior to its annual meeting, a publicly traded company sets a record date and sends out a list of proposals on which shareholders will vote. A shareholder must hold shares as of the record date in order to vote at a shareholder meeting. There are two types of proposals: Management proposals and shareholder proposals. Management proposals—including director elections, audit firm ratification proposals, and proposals regarding the company's executive compensation program (also known as ''say-on-pay'' proposals)—account for 98 percent of proposals and are largely mandated by law or exchange listing requirements. From 2011 to 2017, shareholder proposals accounted for about two percent of proposals but often were more controversial and thus received more attention than management proposals.[81] Shareholder votes on some proposals, such as director elections, are binding. Votes on many other proposals, including shareholder proposals and say-on-pay proposals, are not binding and serve only as shareholder recommendations for the company's board.[82]

1.1. Need for Regulation

As discussed above in section A, Background and Purpose of Regulatory Action, the Department believes that this final rule is necessary to provide clarity and certainty regarding the application of fiduciary obligations of loyalty and prudence with respect to exercises of shareholder rights, including proxy voting. Despite past efforts to make clear fiduciary obligations in this regard, the Department is concerned that its existing sub-regulatory guidance may have inadvertently created the perception that fiduciaries must vote proxies on every shareholder proposal to fulfill their obligations under ERISA. This belief may have caused some fiduciaries to pursue proxy proposals that have no connection to increasing the value of investments used to pay benefits or defray reasonable plan administrative expenses.

For example, some fiduciaries may feel obligated to vote proxies for non-pecuniary proposals related to environmental, social, or public policy agendas. The situation is concerning due to the recent increase in the number of environmental and social shareholder proposals introduced. 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.[83] These proposals increasingly call for disclosure, risk assessment, and oversight, rather than for specific policies or actions, such as phasing out products or activities.[84] The Department believes it is likely that many of these proposals have little bearing on share value or other relation to plan financial interests.[85] The Department also has reason to believe that responsible fiduciaries may sometimes rely on third-party proxy voting advice without taking sufficient steps to ensure that the advice is impartial and rigorous.

The Department's objective in issuing this final rule is to ensure that plan fiduciaries act solely in accordance with the economic interest of the plan and its participants and beneficiaries and consider only pecuniary factors when deciding whether to vote proxies or exercise shareholder rights. The Department believes that addressing these issues in the final rule will help safeguard the interests of participants and beneficiaries in their plan benefits.

1.2. Affected Entities

This final rule would affect ERISA-covered pension, health, and other welfare plans that hold shares of corporate stock. It would affect plans with respect to stocks they hold directly, as well as with respect to stocks they hold through ERISA-covered intermediaries, such as common trusts, master trusts, pooled separate accounts, and 103–12 investment entities. The final rule would not affect plans with respect to stock held through registered investment companies, because the final rule does not apply to such funds' internal management of such underlying investments. The final rule also does not apply to voting, tender, and similar rights with respect to securities that are passed through pursuant to the terms of an individual account plan to participants and beneficiaries with accounts holding such securities.

ERISA-covered plans with 100 or more participants (large plans) annually report data on their stock holdings on Form 5500 Schedule H (see Table 1). Approximately 27,000 defined contribution plans and 5,000 defined benefit plans, with approximately 84 million participants, either hold common stocks or are an Employee Stock Ownership Plan (ESOP). Additionally, 573 health and other welfare plans file the schedule H and report holding common stocks either directly or indirectly. In total, large pension plans and welfare plans hold approximately $1.7 trillion in stock value. Common stocks constitute about 25 percent of total assets of those pension plans that are not ESOPs and hold common stock. Out of the 25,400 pension plans that hold common stock and are not ESOPs, about 20,000 plans hold common stock through an ERISA-covered intermediary and approximately 3,500 plans hold common stock directly. A smaller number of plans hold stock both directly and indirectly.[86] In total, there are approximately 32,000 plans holding either common stock or employer stock, comprised of large plans, welfare plans, and ESOPs. In addition to the large pension plans, approximately 629,000

[79] Department estimates are based on Form 5500 annual reports filed by plans with 100 or more participants. These estimates include only stocks held directly or through Direct Filing Entities, not through mutual funds.

[80] Department calculations are based on U.S. Federal Reserve statistics. Board of Governors of the Federal Reserve System, *Financial Accounts of the United States—Z.1* (Sept. 2020).

[81] Morris Mitler, Dorothy Donohue & Sean Collins, *Proxy Voting by Registered Investment Companies, 2017,* Investment Company Institute Research Perspective (July 2019), at 4 (hereinafter ''ICI Proxy Voting Report'').

[82] *Id.,* at 6; *see also* 15 U.S.C. 78n–1.

[83] *Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a–8,* 84 FR 66458, 66491 (Dec. 4, 2019).

[84] *See* 2019 ISS Proxy Voting Trends, *supra* note 20.

[85] *See* John G. Matsusaka, Oguzhan Ozbas, & Irene Yi, *Can Shareholder Proposals Hurt Shareholders? Evidence from SEC No-Action Letter Decisions,* U.S.C. CLASS Research Paper No. CLASS17–4 (2019), *https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2881408,* at 25; Joseph P. Kalt, L. Adel Turki, Kenneth W. Grant, Todd D. Kendall & David Molin, *Political, Social, and Environmental Shareholder Resolutions: Do They Create or Destroy Shareholder Value?,* National Association of Manufacturers (June 2018), *www.shopfloor.org/wp-content/uploads/2018/06/nam_shareholder_resolutions_survey.pdf.*

[86] DOL estimates from the 2018 Form 5500 Pension Research Files.

small pension plans hold assets and some may invest in stock.[87]

TABLE 1—NUMBER OF PENSION AND WELFARE PLANS HOLDING COMMON STOCKS OR ESOP BY TYPE OF PLAN, 2018 [a]

Common Stock (no employer securities)	Defined benefit	Defined contribution	Total pension plans	Welfare plans	Total all plans
Direct Holdings Only	1,272	2,286	3,558	569	4,127
Indirect Holdings Only	2,792	17,591	20,383	3	20,386
Both Direct and Indirect	941	586	1,527	1	1,528
Total	5,005	20,463	25,468	573	26,041
ESOP (No Common Stock)		5,809	5,809		5,809
Common Stock and ESOP		591	591		591
Total All Plans Holding Stocks	5,005	26,863	31,868	573	32,441

[a] DOL calculations from the 2018 Form 5500 Pension Research Files.

While this final rule would directly affect ERISA-covered plans that possess the relevant shareholder rights, the activities covered under the final rule would be carried out by responsible fiduciaries on plans' behalf. Many plans hire asset managers to carry out fiduciary asset management functions, including proxy voting. In 2018, large ERISA plans reportedly used approximately 17,800 different service providers, some of whom provide services related to the exercise of plans' shareholder rights. Such service providers include trustees, trust companies, banks, investment advisers, and investment managers.[88]

In addition, this final rule will indirectly affect proxy advisory firms.[89] Currently, this market is dominated by two firms: Institutional Shareholder Services, Inc. (ISS) and Glass, Lewis & Co., LLC (Glass Lewis). It has been estimated that in 2013, the combined market share of these two firms was 97 percent (61 percent for ISS and 36 percent for Glass Lewis).[90] Each year, ISS covers approximately 44,000 shareholder meetings and executes 10.2 million ballots on behalf of clients holding 4.2 trillion shares. Glass Lewis covers about 20,000 shareholder meetings annually and provides services to more than 1,300 clients that collectively manage more than $35 trillion in assets.[91]

ERISA plans' demand for proxy advice might decline if fiduciaries refrain from voting shares under the provisions of this final rule or under proxy voting policies adopted pursuant to the safe harbors provided in paragraphs (e)(3)(i)(A) and (B). Plan fiduciaries may want customized recommendations about which particular proxy proposals would have a material effect on the investment performance of their particular plan and how they should cast their vote. Plans' preferences for proxy advice services could shift to prioritize services offering more rigorous and impartial recommendations. These effects may be more muted, however, if the SEC rule amendments enhance the transparency, accuracy, and completeness of the information provided to clients of proxy voting firms in connection with proxy voting decisions.

1.3. General Comments on the Proposed Regulatory Impact Analysis

Comments on the proposed regulatory impact analysis included comments that supported the proposal and others that challenged the Department's analytical approach, assumptions, and conclusions, including criticizing the Appendix A ''illustrative'' analysis as a fundamentally flawed approach to the measurement of possible costs, benefits, and transfers associated with the proposed rule.

As noted, a few commenters agreed with the Department's conclusion that the rule would provide certainty to plan administrators and benefits ERISA plan participants by eliminating the misunderstanding that exists among some stakeholders that ERISA fiduciaries are required to vote all proxies rather than only proxies determined to have a net positive economic impact on the plan analysis. One commenter stated that outside of clear cases of economic gain, the benefits of proxy voting ''are dubious at best.'' Another commenter dismissed the argument that the benefits of shareholder engagement may include realizing gains over the long term and asserted that short-term costs are non-trivial and long-term future benefits are highly speculative. A commenter stated that the rule will add elements of transparency and accountability to the proxy voting process.

Many commenters, however, challenged the Department's proposed Regulatory Impact Analysis and criticized the Department's analysis of the relevant literature.

With respect to the literature, commenters criticized DOL's assertion that the evidence on the effectiveness of and benefits from proxy voting is ''mixed.'' The Department continues to believe that the research studies have a wide range of findings. Some studies have found that the adoption of shareholder proposals has a positive effect on financial performance. For example, Dimson, Karakas, and Li's research, which examines U.S. public companies, finds that the adoption of ESG shareholder proposals increases the returns of companies.[92] Flammer's research, which examines shareholders proposals of U.S. publicly traded companies, also finds that the adoption of shareholder proposals related to corporate social responsibility improves the financial performance of

[87] The Form 5500 does not require these plans to categorize the assets as common stock, so the Department does not know if they hold stock.

[88] DOL estimates are derived from the 2018 Form 5500 Schedule C.

[89] One commenter pointed out that in a proprietary survey of the largest pension funds and defined contribution plans, approximately 92 percent of the respondents indicated that they have formally delegated proxy voting responsibilities to another named fiduciary (*e.g.,* an Investment Manager), and approximately 42 percent of respondents engage a proxy advisory firm (directly or indirectly) to help with voting some or all proxies.

[90] Glassman, James K., and J.W. Verret, ''How to Fix our Broken Proxy Advisory System.'' Arlington, VA: Mercatus Center (2013).

[91] Exemptions from the Proxy Rules for Proxy Voting Advice, 85 FR 55082 (Sept. 3, 2020) (2020 SEC Proxy Voting Advice Amendments).

[92] Dimson, Elroy, Oğuzhan Karakaş, and Xi Li., *Active Ownership,* 28 *The Review of Financial Studies* 12 (2015).

companies.[93] In addition, Martin's research finds that the adoption of shareholder proposals relating to corporate social responsibility increases the returns and market share of companies.[94] Finally, Cuñat, Giné, and Guadalupe's research, which examines shareholder proposals filed with the SEC, finds that adoption of shareholder proposals relating to executive pay improves the market value and the long-term profitability of firms.[95] In contrast, other studies have found shareholder proposals to have a negative effect on financial performance. Cai and Walking's research finds that the announcement of labor-sponsored shareholder proposals results in a negative market reaction.[96] Prevost and Rao's research finds that firms that receive shareholder proposals for the first time experience transitory declines in market returns, while firms that repeatedly receive shareholder proposals experience permanent declines in market returns.[97] In addition, Larcker, McCall, and Ormazabal's research, which examines Russell 3000 companies, finds that changes in compensation contracts made to comply with proxy advisor voting policies results in a negative stock market reaction.[98] Finally, Woidtke's research, which examines Fortune 500 companies, finds that an increase in shareholder activism by public pension funds is negatively associated with stock returns.[99] Furthermore, there are studies with inconclusive results. Karpoff, Malatesta, and Walking's research finds that shareholder proposals have a negligible effect on the share values and operating returns of firms.[100] Wahal's research, which examines firms targeted by pension funds with a social agenda, finds that firms that receive proxy proposals do not experience significant abnormal returns.[101] Wahal's research also finds no evidence of long-term improvement in the performance of the firm.[102] Similarly, Del Guercio and Hawkins' research, which examines firms that received shareholder proposals from large pension funds, finds no evidence of significant abnormal long-term returns.[103] Smith's research, which also examines firms targeted by CalPERS, finds that there is no statistically significant change in the operating performance.[104]

With respect to the Department's analysis, assumptions, and conclusions, although several commenters noted that the costs and benefits associated with a proxy vote are highly uncertain and difficult to quantify, commenters argued that the Department's analysis overstated the current costs of proxy voting, understated the new costs that ERISA plans will incur if the proposal were finalized, and neglected to account for benefits to proxy voting that the proposal would appear to classify as non-economic in nature yet have been linked to better financial performance. One commenter cited the research of a team of academics that found benefits of shareholder voting for the market value of shares.[105]

Many commenters asserted that the proposed rule will discourage voting, and some suggested that less proxy voting by ERISA investors will increase the influence of non-ERISA investors. Several of the commenters expressed concerns that the costs imposed by the rule would cause fiduciaries not to vote proxies, even when economically beneficial, or to adopt the permitted practices described in the proposal which they argued would benefit corporate management at the expense of plan participants and beneficiaries. A commenter asserted that because abstentions may have the effect of a ''no'' or ''yes'' vote, the rule may tip votes one way or the other.[106] Some commenters argued that having proxy votes cast by individuals who are not experts, for example by activists or hedge fund managers rather than by stable, expert, fiduciary shareholders, would not be in the interests of ERISA beneficiaries. Several commenters stated that the rule could lead to a 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. Several commenters noted that proxy voting serves as an important vehicle for checks and balances to keep corporate management accountable, focused on long-term value creation, and to prevent opportunistic behavior.[107] Another commenter suggested that there is significant uncertainty with respect to the economic impact of any proxy vote and that the proposal's requirement to determine the economic impact of voting proxies requires a level of precision that is inconsistent with the way fiduciaries operate. Other commenters expressed concern about determining whether to vote proxies in relation to ESG issues; many criticized the rule for ignoring academic evidence supporting the pecuniary impact of issues the proposal deemed to be non-economic, such ESG concerns that involve significant risks to companies—such as litigation, reputational harm, or stranded assets—and business activities that cause adverse impacts to individuals, employees, and communities.[108] They argued such

[93] Flammer, Caroline, *Does Corporate Social Responsibility Lead to Superior Financial Performance? A Regression Discontinuity Approach,* 61 *Management Science* 11 (2015).

[94] Martins, Fernando, *Corporate Social Responsibility, Shareholder Value, and Competition.* (2020).

[95] Cuñat, Vicente, Mireia Giné, and Maria Guadalupe, *Say Pays! Shareholder Voice and Firm Performance,* 20 *Review of Finance* 5 (2016).

[96] Cai, Jie, and Ralph A. Walkling., *Shareholders' Say on Pay: Does it Create Value*?, *Journal of Financial and Quantitative Analysis* (2011).

[97] Prevost, Andrew K., and Ramesh P. Rao, *Of What Value are Shareholder Proposals Sponsored by Public Pension Funds,* 73 *Journal of Business* 2 (2000).

[98] Larcker, David F., Allan L. McCall, and Gaizka Ormazabal, *Outsourcing Shareholder Voting to Proxy Advisory Firms,* 58 *Journal of Law and Economics* 18 (2015).

[99] Woidtke, Tracie, *Agents Watching Agents?: Evidence from Pension Fund Ownership and Firm Value,* 63 *Journal of Financial Economics* 1 (2002).

[100] Karpoff, Jonathan M., Paul H. Malatesta, and Ralph A. Walkling, *Corporate Governance and Shareholder Initiatives: Empirical Evidence,* 42 *Journal of Financial Economics* 3 (1996).

[101] Wahal, Sunil, Pension Fund Activism and Firm Performance, *Journal of Financial and Quantitative Analysis* (1996).

[102] *Id.*

[103] Del Guercio, Diane, and Jennifer Hawkins, *The Motivation and Impact of Pension Fund Activism,* 52 *Journal of Financial Economics* 3 (1999).

[104] Smith, Michael, *Shareholder Activism by Institutional Investors: Evidence from CalPERS,* 51 *Journal of Finance* 1 (1996).

[105] Vicente Cuñat & Mireia Giné & Maria Guadalupe, 2012. ''The Vote Is Cast: The Effect of Corporate Governance on Shareholder Value,'' *Journal of Finance;* Vicente Cuñat & Mireia Giné & Maria Guadalupe, 2016. ''Say Pays! Shareholder Voice and Firm Performance,'' Review of Finance, European Finance Association, vol. 20(5), at 1799–1834.

[106] Data on abstentions not tipping votes is suggestive, but not definitive. Figure 9 of the ICI's 2017 research on proxy voting (*www.ici.org/pdf/per25-05.pdf*), indicates that the percentage of shares voting ''for'' various proposals (the overwhelming number of which were management proposals) as 95.2% in favor of management proposals and 29.2% in favor of shareholder proposals. The data is aggregated for all votes and not focused on specific proposals, which could indicate that there are no close votes or at least some close votes which could be tipped. Based on this uncertainty, the Department cannot quantify the number of close votes that could be tipped based on the available data, especially for shareholder proposals. While the Department received multiple comments expressing concern that the rule would make it more difficult to reach a quorum, the commenters did not include any data supporting this assertion, and the Department is not aware of any data sources that would support a qualitative or quantitative analysis of the final rule's impact on reaching a quorum.

[107] For the CFA Institute Code of Ethics and Standards of Professional Conduct and the CFA Institute Corporate Governance Manual, please see *www.cfainstitute.org/en/ethics-standards/ethics/code-of-ethics-standards-of-conduct-guidance.*

[108] Some commenters cited a 2015 survey by the CFA Institute that reported that 73 percent of global investors take ESG factors into account in their investment analysis and decisions. They also refer to a McKinsey study that reports that ESG

Continued

matters are critical to performing due diligence risk analysis and have become increasingly germane to assessing company strategy and long-term financial viability. One commenter criticized the Department for allowing the permitted practice of voting with management but not allowing a similar permitted practice of voting with proxy advisors. The commenter asserted that voting with proxy advisors costs less and that proxy advisors are subject to fewer and less severe conflicts than management.

Finally, some commenters focused specifically on proxy advisory firms. Some commenters disagreed with the Department's expectation that the rule may reduce plans' demand for proxy advice. A commenter pointed to a report from the Manhattan Institute that suggested that some ERISA fiduciaries are using proxy advisors as a low-cost way of meeting their own fiduciary voting obligations, despite the fact that the proxy advisor firms themselves are not held to a fiduciary standard. One commenter argued that proxy advisors are in a resource-constrained environment that adversely affects the advice they provide. In support, the commenter cites a study suggesting that ISS provides lower quality advice during the proxy season, when the firm is at its busiest, and higher quality advice during other times. This result suggests that during the busy proxy season, when proxy advisor firms' resources are most constrained, such firms are unable to maintain the same quality of service as provided during other periods.

After reviewing the public comments, the Department agrees that there is uncertainty regarding the costs and benefits of proxy voting activities of ERISA plans, both currently and under the terms of the proposed regulation. The Department presented an illustration of an analytical approach to evaluating the possible impacts of the proposed rule. The Department presented the data it had to estimate the impacts of the rule and also highlighted places where it lacked data to accurately measure key parameters. In so doing, the Department solicited comments and data to allow the accurate estimation of the impact of the rule's requirement and the permitted practices. The Department received comments on the illustration and its assumptions that sought to estimate the costs of the proposed rule. Commenters did not provide explicit data or estimates for a per vote burden to conduct research or required documentation, nor did they provide alternative estimates of the number of proxies that would be impacted by the proposal. Thus, notwithstanding the solicitation of such data, the Department still lacks critical information that would allow it to use or modify the model to try to produce a more accurate measure of the cost of the final rule's requirements.

The Department included the illustration to solicit public input on one possible way to envision and quantify the potential cost burden and costs savings that could be associated with the proposal. The Department emphasized that the illustration was based on speculative assumptions due to insufficient data, and, as noted above, many of the commenters criticized its basis. Based on the public comments and the fact that commenters did not provide data or estimates that would support continued use of the illustration as part of this final regulatory impact analysis, the Department has concluded that the illustrative analysis that was presented for public comment as part of the proposal does not represent a reliable construct for evaluating the costs, benefits, and transfers associated with the final rule. Perhaps more importantly, however, as discussed above and below, the Department has made substantial changes to the proposed rule that have reduced much of the cost burden associated with the final rule and thus the illustrative analysis, even with its challenges identified by the commenters, no longer reflects the potential burdens associated with the rule.

1.4. Benefits

This final rule would benefit plans by providing improved guidance regarding how ERISA's fiduciary duties apply to proxy voting. As discussed above, sub-regulatory guidance that the Department has previously issued over the years may have led to a misunderstanding among some that fiduciaries are required to vote on all proxies presented to them. This misunderstanding may have led some plans to expend plan assets unnecessarily to research and vote on proxy proposals not likely to have a pecuniary impact on the value of the plan's investments. The final rule is intended to eliminate that confusion and includes specific language in paragraph (e)(2)(ii) clearly stating that plan fiduciaries do not have an obligation to vote all proxies. The rule also includes a ''safe harbor'' provision under which plan fiduciaries may adopt proxy voting policies and parameters prudently designed to serve the plan's economic interest. This will encourage ERISA fiduciaries to execute shareholder rights in an appropriate and cost-efficient manner.

The final rule clarifies the duties of fiduciaries with respect to proxy voting and the monitoring of proxy advisory firms. Specifically, in order to meet their fiduciary obligations to manage shareholder rights, plan fiduciaries must (i) act solely in accordance with the economic interest of the plan and its participants and beneficiaries considering the impact of any costs involved; (ii) 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 promote non-pecuniary benefits or goals; and (iii) prudently monitor the proxy voting activities of investment managers or proxy advisory firms to whom that authority to vote proxies or exercise shareholder rights has been delegated.

Accordingly, plan fiduciaries will be better positioned to conserve plan assets by having clear direction and the option to prudently adopt voting policies that (i) focus voting resources only on particular types of proposals that the fiduciary has prudently determined are substantially related to the issuer's business activities or are expected to have a material effect on the value of the investment; and (ii) refrain from voting on proposals or particular types of proposals when the plan's holding in a single issuer relative to the plan's total investment assets is below a quantitative threshold that the fiduciary prudently determines, considering its percentage ownership of the issuer and

companies create value disproportionate to their peers. Similarly, by citing many studies made by the investment industry, some commenters asserted that there is a substantial, and growing, body of empirical research that has identified meaningful links between a company's ESG characteristics and financial performance. These include studies produced by MSCI, Bank of America Merrill Lynch, Allianz Global Investors, Nordea Equity Research, Goldman Sachs, Morningstar, and Deutsche Asset & Wealth Management. Some commenters cited an academic study that uses ISS and FactSet data to present evidence of a positive causal effect of the passing of corporate social responsibility shareholder proposals, the ones that are presumably tied to ESG investing motives, to the correspondent shareholder returns. Martins, Fernando, *Corporate Social Responsibility, Shareholder Value, and Competition* (July 1, 2020). Available at *SSRN: https://ssrn.com/abstract=3651240* or *http://dx.doi.org/10.2139/ssrn.3651240.* The same commenter cited an observational study that reaches the same conclusion: *www.hbs.edu/faculty/conferences/2013-sustainability-and-corporation/Documents/Active_Ownership_-_Dimson_Karakas_Li_v131_complete.pdf.* One commenter referred to a meta-study showing that there is a correlation between sustainability business practices and economic performance. Clark, Gordon L. and Feiner, Andreas and Viehs, Michael, From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance (March 5, 2015). Available at SSRN: *https://ssrn.com/abstract=2508281* or *http://dx.doi.org/10.2139/ssrn.2508281.*

other relevant factors, is sufficiently small that the matter being voted upon is not expected to have a material effect on the investment performance of the plan's portfolio. Thus, votes will be cast that more frequently advance plans' economic interests. Cost savings and other benefits to plans would flow to plan participants and beneficiaries and plan sponsors.

The final rule will replace existing guidance on fiduciary responsibilities for exercising shareholders' rights. The final rule will provide more certainty than the existing sub-regulatory guidance, and unlike such guidance, the final rule sets forth binding, specific requirements.

The final regulation could increase investment returns on plan assets by specifying when plan fiduciaries should or should not exercise their shareholder rights to vote proxies. Plan fiduciaries are responsible for maximizing the economic benefits to the plan, including in their management of proxy voting rights, which may involve voting proxies or declining to vote them. If the cost of obtaining information that informs the vote exceeds the likely economic benefits to the plan of voting, then fiduciaries should not vote. This course of action will save resources and increase societal benefits.

The resources freed for other uses due to voting fewer proxies (minus potential upfront transition costs) would represent benefits of the rule. To the extent that the final regulation increases the investment return on plan assets, it would enhance participants' and beneficiaries' retirement security, thereby strengthening a central purpose of ERISA. For the plans and participants that would be affected by the final rule, the benefits they would experience from higher investment returns, compounded over many years, could be considerable.

The increased returns would be associated with investments generating higher pre-fee returns, which means the higher returns qualify as benefits of the rule. However, to the extent that there are any externalities, public goods, or other market failures, those might generate costs to society on an ongoing basis. For example, a fiduciary may vote for a proposal on a corporate merger or acquisition transaction to maximize shareholder value even though implementation of the proposal would bring about impacts in an affected geographic area that would be adverse for local businesses or residents. Finally, some portion of the increased returns would be associated with transactions in which there is an opposite party experiencing a decreased return of equal magnitude. This portion of the rule's impact would, from a society-wide perspective, be appropriately categorized as a transfer as discussed further in the Transfers section below (though it should be noted that, if there is evidence of wealth differing across the transaction parties, it would have implications for marginal utility of the assets).

1.5. Costs

The Department received several comments regarding estimated costs for the proposed rule. Commenters were divided in their opinions about whether the illustration over or under estimated the proposed rule's total costs.

Several commenters expressed concern that the rule will increase plan costs. One commenter said that conducting a cost-benefit analysis for each vote is ''unworkable'' and will ''create a dramatic cost burden.'' Some commenters asserted that the proposed rule would substantially increase costs because the commenters claimed that the current cost to vote proxies was small, with one commenter even suggesting it was approaching zero. Other commenters argued that the Department's cost estimates were suspect because the Department estimates that saving resulting from adopting the proposal's permitted practices were significantly larger than the entire revenues of the proxy advisory market. One commenter suggested their cost to provide services would increase by 10 to 20 times their current rate. Other commenters pointed out that although the model showed large costs, actual costs would be even larger, approaching $13 billion a year.

A few of the commenters criticized that the rule places a higher emphasis on short-term costs and performance, as the short-term economic impact is often easier to quantify with less uncertainty. The commenters argued that this would lead fiduciaries to focus on short-term economic implications at the expense of long-term value, which some commenters argued would be in violation of a fiduciary's duty.

One commenter stated the proposal was onerous and that it may not even be possible for a plan fiduciary to do the proposal's mathematical exercises to determine the economic impact, let alone defend the determination, of every proxy vote in a detailed way and document it. The commenter felt this would raise the costs of even routine proxy votes. The commenter also said plans may need to hire additional service providers to help determine the economic impact on the plan of each vote. The need to have additional reviews and recordkeeping procedures would increase costs for voting analysis. Several commenters noted that the Department's economic analysis overlooked costs associated with the proposed rule, such as the cost of analyzing whether to abstain from a vote and the overhead costs of voting with management.

A commenter said plans do not have the expertise nor the desire to vote the proxies themselves but instead rely on asset managers. The commenter suggested the proposed rule would make proxy advisory services more expensive, and the need to independently investigate the basis of the proxy advisor's recommendation will be costly. Another commenter reported that they would need to charge a rate 10 to 20 times the firm's current rate due to the proposal. The commenter stated that such a high cost to vote would force plans to either not vote or defer to management.

Another commenter expressed the view that the cost to use ERISA 3(38) investment managers will increase as they will have to bifurcate their processes, policies, and voting to accommodate ERISA and non-ERISA accounts. Additionally, the commenter argued that institutional investors already approach their proxy voting methodically and professionally.

Several commenters noted that the analysis failed to address opportunity costs or externalities. With reference to externalities, one commenter referred to academic research on corporate voting and elections that highlights the voters' motivation of communication with the board of directors.[109] According to this research, voting can be used as a channel of communication with boards of directors, and protest voting can lead to significant changes in corporate governance and strategy. In such scenarios, voting success would not only be assessed by examining the returns to individual targeted firms' stocks, but also by the impact on the behavior of other companies throughout their portfolios. Another commenter noted, as an example of a negative externality, a study by Arjuna Capital that emphasized the negative environmental effects of carbon

[109] David Yermack, *Shareholder Voting and Corporate Governance,* 2 Ann Rev. Fin. Econ. 2.1, 2.15 (2010); Frederick Alexander, *The Benefit Stance: Responsible Ownership in The Twenty-First Century, 36* Oxford Rev. Econ Policy 341, 355 (2020); Robert G. Hansen and John R. Lott, *Externalities and Corporate Objectives in a World with Diversified Shareholder/Consumers,* Journal Of Financial And Quantitative Analysis, 1996, vol. 31, issue 1, 43–68.

emissions, which could potentially be addressed through proxy voting.[110]

One commenter stated they currently incur minimal costs to execute proxy votes in a way that they believe best protects the interests of participants and beneficiaries. Another commenter said that any increased costs would be minimal and suggested that to ensure the rule imposes a minimal burden on plan managers and proxy advisory firms, the Department could allow these firms to make the data used for voting shareholder decisions publicly available for external economic analysis, allowing academics, think tanks, and concerned citizens to provide additional economic analysis.

Finally, commenters expressed concern that by requiring plan fiduciaries to determine economic materiality and to document that determination, the proposed rule would increase litigation risk for plan fiduciaries. A few of the commenters specifically alluded to increased litigation risk from plan participants, alleging improper voting activity. Some of the commenters stated that this risk would discourage plan fiduciaries to vote proxy votes.

After carefully considering such comments, the Department made several modifications to the proposed rule. The most significant adjustment from the proposal results from the Department's agreement with the recommendation of some commenters that the final rule take a more principles-based approach to this subject matter. The Department estimates that the more principles-based approach will reduce much of the cost burden associated with the proposed rule. As discussed earlier in this preamble, the most significant revision in the final rule eliminates paragraphs (e)(3)(i) and (ii) from the proposal.

Paragraph (e)(3)(i) of the proposal provided 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 those factors described in paragraph (e)(2)(ii) of the proposal and taking into account the costs involved (including the cost of research, if necessary, to determine how to vote). Paragraph (e)(3)(ii) of the proposal provided that 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 after considering those factors described in paragraph (e)(2)(ii) of the proposal and taking into account the costs involved.

As stated above, commenters criticized these provisions of the proposal as requiring a fiduciary to undertake an economic impact analysis in advance of each issue that is the subject of a proxy vote in order to even consider voting. A commenter further noted that a fiduciary may not discover until after the analysis is performed that the cost involved in determining whether to vote outweighs the economic benefit to the plan.

The Department is persuaded by the comments that the requirements contained in paragraphs (e)(3)(i) and (ii) of the proposal should not be incorporated in the final rule. The Department recognizes the concerns expressed regarding potential increased costs and liability exposure, as well as potential risks to plan investments that could result from fiduciaries not voting when prudent to do so. Due to this and other changes the Department has made in the final rule that are discussed above, the Department expects that the incremental costs of the final rule provisions will be minimal on a per-plan basis.

The Department recognizes that plans will need to spend time reviewing the final rule, evaluating how it affects their proxy voting practices, and implementing any necessary changes. The Department estimates that this review process will require a lawyer to spend approximately four hours to complete, resulting in a cost burden of approximately $34.3 million.[111] The Department believes that these processes will likely be performed for most plans by a service provider that likely oversees multiple plans. Therefore, the Department's estimate likely represents an upper bound, because it is based on the number of affected plans. The Department does not have sufficient data that would allow it to estimate the number of service providers acting in such a capacity for these plans.

The Department believes that many fiduciaries already are compliant with the final rule, because they are meeting the requirements of the Department's sub-regulatory guidance and prudently conducting their business operations to satisfy their fiduciary obligations as required by ERISA.[112] The Department acknowledges that such practices are not universal. In the course of its enforcement activity, the Department sometimes encounters instances where documentation is absent or does not meet the requirements of this final rule. The Department additionally believes that the availability of economies of scale limits the costs of this final rule. The Department understands that under the final rule, 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. The Department estimates that plan fiduciaries or investment managers will require a half hour annually and a half hour of help from clerical staff to maintain or document the required information, resulting in an annual cost burden estimate of $6.05 million.[113] For a more in-depth discussion on the costs for maintaining the required documentation, please refer to the Paperwork Reduction Act section of this document below.

Several of the commenters noted that the Department failed to recognize the additional costs associated with developing or updating policies or procedures to reflect the requirements of the proposed rule. One commenter, however, asserted that most fiduciaries have thoughtful proxy policies. Another commenter stated that, contrary to the DOL assumption that there are ''cost savings'' because of the provisions in the rule that allow the adoption of proxy voting policies, proxy voting policies already exist and the rule would impose additional costs because such policies will need to be reviewed on an initial and ongoing basis. After further deliberation, the Department agrees that plans are likely to incur such costs, particularly plans that choose to adopt the safe harbors contained in paragraphs (e)(3)(i)(A) and (B) of the final rule. The Department believes that the final rule largely comports with industry practice for ERISA fiduciaries; therefore the Department estimates that on average, it will take a legal professional two hours to update policies and procedures for each of the estimated 63,911 plans affected by the rule. This results in a cost of $17.2 million in the first year.[114]

[110] *See http://arjuna-capital.com/wp-content/uploads/2016/07/Climate_Change_from_the_Investor_s_Perspective.pdf.*

[111] The burden is estimated as follows: (63,911 plans * 4 hours) = 255,644 hours. A labor rate of $138.41 is used for a lawyer. The cost burden is estimated as follows: (63,911 plans * 4 hours * $138.41) = $34,309,915.

[112] 29 CFR 2509.2016–01 (81 FR 95879, Dec. 29, 2016).

[113] The burden is estimated as follows: 63,911 plans * 0.5 hours = 31,955.4 hours for both a plan fiduciary and clerical staff. A labor rate of $134.21 is used for a plan fiduciary and a labor rate of $55.14 for clerical staff (31,955.4 * $134.21 = $4,288,739 and 31,955.4 * $55.14 = $1,762,023).

[114] The burden is estimated as follows: 63,911 plans * 2 hours = 127,821.8. A labor rate of $134.21

The requirement in paragraph (e)(3)(ii) to periodically review proxy voting policies already is required for fiduciaries to meet their obligations under ERISA; therefore, the Department does not expect that plans will incur additional cost associated with the periodic review.

The Department generally does not expect that this final rule will change the costs associated with plans' remaining voting activity. Provisions requiring responsible fiduciaries to monitor and document voting policies and activities would generally be satisfied by current best practices that satisfy earlier Departmental guidance. Neither does the Department expect plans to incur substantial costs from proxy advisory firms' potential efforts to help fiduciaries meet the final rule's requirements. If they do not already meet the standards detailed in the final regulation, plans that currently exercise shareholder rights, including proxy voting activities, will incur the costs associated with deciding whether to exercise shareholder rights pursuant to this final rule. The Department, however, does not have sufficient information to document such costs.

It is possible that proxy advisory firms would take steps to avoid or mitigate conflicts of interest, strengthen factual and analytic rigor, better match their research and recommendations with ERISA plans' interests, or increase transparency as a result of the final rule. The Department notes, however, that proxy advisory firms are likely to take at least some of these steps in response to recent SEC policy initiatives and spread their related costs across all of their clients, not just ERISA plans.[115] At the same time, the final rule may reduce plans' demand for proxy advice. However, this reduction in demand is beneficial to plans as they previously were purchasing more advice than they would have otherwise chosen due to their misunderstanding that they were required to vote all proxies. This reduced demand will lower the market price and the amount of advice purchased. Consequently, any compliance costs passed on from proxy advisory firms to ERISA plans are likely to be at least partially offset by plans' cost savings from purchasing a smaller amount of advice. It should be noted that proxy advisory firms will see a reduction in revenues as a result of the decreased demand for their services. In addition, proxy advisory firms' efforts to satisfy any SEC requirements might ease responsible fiduciaries' efforts to comply with this final rule. For example, it may be easier to monitor proxy advisory firms if those firms provide additional disclosure about their conflicts of interest and their policies and procedures to address such conflicts.

The Department estimates that the final rule would impose incremental costs of approximately $57.52 million in the first year and $6.05 million in subsequent years. Over 10 years, the associated costs would be approximately $90.6 million with an annualized cost of $12.90 million, using a seven percent discount rate.[116] Using a perpetual time horizon (to allow the comparisons required under Executive Order 13771), the annualized costs in 2016 dollars are $6.76 million at a seven percent discount rate.[117]

1.6. Transfers

Proxy advisory firms that respond best to this final rule will likely gain a relative competitive advantage. Firms that limit or eliminate conflicts of interest and modify their services to better align with the guidance of these final regulations could gain market share relative to firms that do not. Firms that are willing to tailor their voting guidelines, strategies, and costs according to each plan's investment guidelines could gain market share relative to firms that do not.

The final rule may reduce plans' demand for proxy advice, lowering the market price, the amount of advice purchased, and revenues. This represents a transfer from proxy advisory firms to plans, who will benefit as they previously were purchasing more advice than they would have chosen to due to their misunderstanding that plan fiduciaries were required to vote all proxies.

The Department also notes, however, that the market for proxy advisors could also change as a result of the final rule. Such changes could lead to increased competition among proxy advisory firms. In such a scenario, it is possible that the rule will result in a reduction in the expenses plans incur to purchase proxy advisory services. Although the Department does not have sufficient data to quantify this possibility, it would result in a transfer from proxy advisory firms to plans.

Moreover, as noted previously, if some portion of rule-induced increases in returns would be associated with transactions in which the opposite party experiences decreased returns of equal magnitude, then this portion of the final rule's impact would, from a society-wide perspective, be appropriately categorized as a transfer.

1.7. Regulatory Alternatives

As discussed above, the Department considered retaining paragraphs (e)(3)(i) and (ii) of the proposal. Paragraph (e)(3)(i) of the proposal provided 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 those factors described in paragraph (e)(2)(ii) of the proposal and taking into account the costs involved (including the cost of research, if necessary, to determine how to vote). Paragraph (e)(3)(ii) of the proposal provided that 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 after considering those factors described in paragraph (e)(2)(ii) of the proposal and taking into account the costs involved.

After carefully considering comments, the Department was persuaded to eliminate paragraphs (e)(3)(i) and (ii) and adopt a more principles-based, less prescriptive approach in the final rule that will reduce much of the cost burden associated with the proposed rule. Commenters criticized these provisions of the proposal as requiring a fiduciary to undertake an economic impact analysis in advance of each issue that is the subject of a proxy vote in order to even consider voting. A commenter further noted that a fiduciary may not discover until after the analysis is performed that the cost involved in determining whether to vote outweighed the economic benefit to the plan. The Department recognizes the concerns expressed regarding potential increased costs and liability exposure associated with these provisions, as well as potential risks to plan investments

is used for a plan fiduciary: (127,821.8 * $134.21 = $17,154,957).

[115] The SEC's rule amendments require proxy advisory firms engaged in a solicitation to provide conflicts of interest disclosure, to adopt and publicly disclose policies and procedures reasonably designed to ensure that the company subject of the proxy voting advice has such advice made available to it at or prior to the time the advice is disseminated, and to provide a mechanism by which its clients can become aware of any written statements by the company in response to the proxy advice. The SEC also modified its proxy solicitation antifraud rule to specifically include material information about the proxy advisor's methodology, sources of information, or conflicts of interest, as examples of when the failure to disclose could, depending upon the particular facts and circumstances, be considered misleading. *See* 2020 SEC Proxy Voting Advice Amendments, at 242–246.

[116] The costs would be $101.58 million over 10-year period with an annualized cost of $11.91 million, applying a three percent discount rate.

[117] The annualized costs in 2016 dollars would be $6.31 million applying a three percent discount rate.

that could result from fiduciaries not voting when prudent to do so.

1.8. Uncertainty

The Department's economic assessment of this final rule's effects is subject to uncertainty. Specific areas of uncertainty are discussed below:

Cost Savings—As noted earlier, the Department 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. Many of the commenters criticized that the Department lacks data and evidence to support its cost-benefit analysis and remarked that the Department should not move forward with the rule until the associated costs and benefits are more certain. The Department firmly disagrees and believes that the impact of the rule has been reasonably assessed based on the best available data.

Demand for New Services—The Department solicited comments regarding whether the final rule would create a demand for new services, and if so, what alternate services or relationships with service providers might result and how overall plan expenses could be impacted. The Department did not receive comments that specifically addressed this question.

Other Securities—The final rule will generally govern plans' exercise of shareholder rights appurtenant to their stock holdings of individual companies, but not to their holdings of other securities. The Department cannot determine whether some plans nonetheless would modify their practices with respect to other securities because of this final rule. As noted earlier, ERISA pensions held just 5.5 percent of total corporate equity in 2019, down from a high of 22 percent in 1985. Mutual funds, in contrast, held 22 percent of all corporate equity in 2019, up from 6 percent in 1985.[118] As ERISA-covered pensions have shifted from defined benefit to defined contribution plans, both the proportion of pension assets invested in mutual funds and the proportion of all mutual fund shares owned by pensions have increased dramatically. In 2019, ERISA-covered pensions held 25 percent of all mutual fund shares, up from 8 percent in 1985. ERISA would apply to any proxy votes for mutual fund shares and shares of other funds registered with the SEC for which the plan fiduciary is responsible. ERISA does not govern the management of the portfolio internal to a fund registered with the SEC, including such fund's exercise of its shareholder rights appurtenant to the portfolio of stocks it holds, though ERISA would apply to similar funds organized as collective investment trusts. One commenter stated that if plans do not participate in the proxy process, it may prevent issuers from reaching quorum for their shareholder meetings, and this would impose costs on plans.

Non-ERISA Investors—Many asset managers serve both ERISA plans and other investors. The Department believes such uniform voting for ERISA and non-ERISA clients may sometimes jeopardize responsible fiduciaries' satisfaction of their duties under ERISA. However, as noted earlier in the preamble, this 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 interests ahead of their client's.[119] Where an SEC registered investment adviser has assumed the authority to vote on behalf of its client, the SEC has stated that the investment adviser, among other things, must have a reasonable understanding of the client's objectives and must make voting determinations that are in the client's best interest.

Under this final rule, responsible fiduciaries might increase their demands for asset managers to implement separate policies customized for particular ERISA plans or for ERISA plans generally, such as policies that align with the proposed permitted practices in paragraph (e)(3)(iii). One commenter noted that policies would increase costs for plans and investment without an incremental benefit to participants and beneficiaries. The Department discusses the impact of updating policies and procedures in the cost section above.

Asset Allocation—This final rule could exert influence on a plan's asset allocation. For example, the quantitative threshold provision in paragraph (e)(3)(i)(B) would permit responsible fiduciaries, after prudently considering the relevant factors, to adopt proxy voting policies allowing them to refrain from voting on proposals or particular types of proposals when the plan's holding in a single issuer is sufficiently small relative to the plan's total investment that the outcome of the vote is not expected to have a material impact on the investment performance of the plan's portfolio. This provision might produce additional economic benefits by promoting fuller and more optimal diversification where it may otherwise have been lacking. That is, the quantitative threshold could prompt a fiduciary to diversify what otherwise would have been a concentration of more than the specified threshold amount of a plan's portfolio in a single stock.

Vote Categories—Proxy votes can be tallied in four ways: For, against/withhold, abstain, and not voted. The vast majority of outstanding shares are held in "street name" by intermediaries, such as broker-dealers. 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. If an investor is unsure about a matter or unsure whether her interests and management's interests are aligned, the investor arguably should abstain.

[118] Department calculations based on U.S. Federal Reserve statistics, Financial Accounts of the United States—Z.1.

[119] *See* Commission Interpretation Regarding Standard of Conduct for Investment Advisers, 84 FR 33669, 33673 (July 12, 2019) (discussing an adviser's obligation to make a reasonable inquiry into its client's financial situation, level of financial sophistication, investment experience and financial goals and have a reasonable belief that the advice it provides is in the best interest of the client based on the client's objectives); Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, Release No. IA–5325 (Aug. 21, 2019) (82 FR 47420 (Sep. 10, 2019) (clarifying investment advisers' duties when voting shareholder proxies). *See also* Rule 206(4)–6 under the Investment Advisers Act of 1940, 17 CFR 275.206(4)–6 (Under rule 206(4)–6, it is a fraudulent, deceptive, or manipulative act, practice or course of business within the meaning of section 206(4) of the Investment Advisers Act for an investment adviser to exercise voting authority with respect to client securities, unless the adviser (i) has adopted and implemented written policies and procedures that are reasonably designed to ensure that the adviser votes proxies in the best interest of its clients, which procedures must include how the investment adviser addresses material conflicts that may arise between the adviser's interests and interests of their clients; (ii) discloses to clients how they may obtain information from the investment adviser about how the adviser voted with respect to their securities; and (iii) describes to clients the investment adviser's proxy voting policies and procedures and, upon request, furnishes a copy of the policies and procedures to the requesting client.

1.9. Conclusion

The final rule would benefit ERISA-covered plans, as it provides guidance regarding how ERISA's fiduciary duties apply to proxy voting and in particular when fiduciaries should refrain from voting. Plan fiduciaries will be able to conserve plan assets as they refrain from researching and voting on proposals that are unlikely to have a material effect on the investment performance of the plan's portfolio, and thereby increase the return on plan assets. The Department estimates that the final rule's cost impact is substantially less than the proposal due to significant revisions to the required actions of a plan fiduciary that were made in the final rule in response to comments on the proposal.

2. Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995 (PRA 95) (44 U.S.C. 3506(c)(2)(A)), the Department solicited comments concerning the information collection request (ICR) included in the Fiduciary Duties Regarding Proxy Voting and Shareholder Rights ICR (85 FR 55219). At the same time, the Department also submitted an information collection request (ICR) to the Office of Management and Budget (OMB), in accordance with 44 U.S.C. 3507(d).

The Department received comments that specifically addressed the paperwork burden analysis of the information collection requirement contained in the proposed rule. The Department took into account such public comments in developing the revised paperwork burden analysis discussed below.

In connection with publication of this final rule, the Department is submitting an ICR to OMB requesting approval of a new collection of information under OMB Control Number 1210–0165. The Department will notify the public when OMB approves the ICR.

A copy of the ICR may be obtained by contacting the PRA addressee shown below or at *www.RegInfo.gov.* PRA ADDRESSEE: G. Christopher Cosby, Office of Regulations and Interpretations, U.S. Department of Labor, Employee Benefits Security Administration, 200 Constitution Avenue NW, Room N–5718, Washington, DC 20210; *cosby.chris@dol.gov.* Telephone: 202–693–8410; Fax: 202–219–4745. These are not toll-free numbers.

It has long been the view of the Department that the duty to monitor necessitates proper documentation of the activities that are subject to monitoring.[120] Accordingly, the Department's final rule requires that plan fiduciaries maintain records on proxy voting activities and other exercises of shareholder rights. This requirement applies to all pension plans with investments, including those that have shareholder rights and proxy votes that may need to be exercised.

The Department believes that most plan fiduciaries have followed the Department's prior sub-regulatory guidance or already are performing most if not all of the documentation requirements of the final rule as a prudent practice in their normal course of business. While the incremental burden of the final rule is generally small, perhaps even *de minimis,* the Department discussed the full burden of such requirements below to allow for full evaluation of the requirements in the information collection.

According to the most recent Form 5500 data there are 721,876 pension plans (92,480 large plans and 629,396 small plans) and 8,475 health or welfare plans (5,626 large plans filing a schedule H, and 2,849 small plans filing a schedule I).[121] While the Schedule H collects information on a plan's stock holdings, Schedule I lacks the specificity to determine if small plans hold stocks. As shown in Table 1, 31,868 pension plans hold stocks and would have shareholder rights they may need to exercise. Additionally, 573 health and other welfare plans file the schedule H and report holding either common stocks or employer stocks. The Department lacks information on the number of small plans that hold stock. Small plans are significantly less likely to hold stock than larger plans. For purposes of estimating the burden, five percent of small plans are presumed to hold stock resulting in 31,470 small plans needing to comply with the information collection. Therefore, a total of 63,911 plans will need to comply with this information collection.

2.1. Maintain Documentation

The final rule requires that the named plan fiduciary must maintain records on proxy voting activities and other exercises of shareholder rights. Where the authority to vote proxies or exercise shareholder rights has been delegated to an investment manager pursuant to ERISA section 403(a)(2), or a proxy voting firm or another person performs advisory services as to the voting of proxies, plan fiduciaries must prudently monitor the proxy voting activities of such investment manager or proxy advisory firm and determine whether such activities are consistent with paragraphs (e)(2)(i) and (ii) and (e)(3) of this section.

Much of the information needed to fulfill these requirements is generated in the normal course of business. Plans may need additional time to maintain the proper documentation, but this burden is likely to be reduced by the adoption of policies by plan fiduciaries that incorporate one or more of the final rule's safe harbors.

Commenters expressed concerns that the proposed rule would be onerous, since it would not be feasible for plan fiduciaries to determine the economic impact of every proxy vote in a detailed way and document it. Thus, commenters suggested that the Department underestimated the amount of time that fiduciaries and clerical staff would spend documenting and maintaining documentation for votes. As discussed above in Section 1.5, after carefully considering these comments, the Department was persuaded to adopt a more principles-based, less prescriptive approach in the final rule that does not carry forward specific documentation and recordkeeping provisions in the proposal that were identified by commenters as burdensome and unnecessary. The Department believes that with this revision, the final rule's documentation and recordkeeping requirements should result in less burden than the proposal's requirements, because the final rule requirements mirror previous guidance and align with existing fiduciary duty of documentation.

However, in light of the public comments that argued that the Department underestimated the recordkeeping burden and because of the uncertainty involved in determining which plans will need to change recordkeeping practices to comply with the final rule, the Department is retaining the documentation time estimate from the proposal. This is responsive to the commenters' assertion and is a step intended to avoid underestimating the average time required for plan fiduciaries to comply with the final rule.

The Department estimates that plan fiduciaries or investment managers will require a half hour annually and a half hour of help from clerical staff to maintain or document the required information. This is likely an overestimate, because many, if not most, plans use investment managers. These investment managers provide similar services for many plans. This results in

[120] 29 CFR 2509.2008–2 (73 FR 61731 (Oct. 17, 2008)).

[121] EBSA estimates using 2018 Form 5500 filing data.

an annual cost burden estimate of $6,050,762.[122]

These paperwork burden estimates are summarized as follows:

Type of Review: New collection.

Agency: Employee Benefits Security Administration, Department of Labor.

Title: Fiduciary Duties Regarding Proxy Voting and Shareholder Rights.

OMB Control Number: 1210–0165.

Affected Public: Businesses or other for-profits.

Estimated Number of Respondents: 63,911.

Estimated Number of Annual Responses: 63,911.

Frequency of Response: Occasionally.

Estimated Total Annual Burden Hours: 0.

Estimated Total Annual Burden Cost: $6,050,762.

3. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA)[123] imposes certain requirements with respect to federal rules that are subject to the notice and comment requirements of section 553(b) of the Administrative Procedure Act[124] and are likely to have a significant economic impact on a substantial number of small entities. Unless the head of an agency certifies that a final rule is not likely to have a significant economic impact on a substantial number of small entities, section 604 of the RFA requires the agency to present a final regulatory flexibility analysis of the final rule.[125]

For purposes of analysis under the RFA, the Employee Benefits Security Administration (EBSA) considers employee benefit plans with fewer than 100 participants to be small entities.[126] The basis of this definition is found in section 104(a)(2) of ERISA, which permits the Secretary of Labor to prescribe simplified annual reports for plans that cover fewer than 100 participants. Under section 104(a)(3) of ERISA, the Secretary may also provide for exemptions or simplified annual reporting and disclosure for welfare benefit plans. Pursuant to the authority of section 104(a)(3), the Department has previously issued (see 29 CFR 2520.104–20, 2520.104–21, 2520.104–41, 2520.104–46, and 2520.104b–10) simplified reporting provisions and limited exemptions from reporting and disclosure requirements for small plans, including unfunded or insured welfare plans, that cover fewer than 100 participants and satisfy certain requirements. While some large employers have small plans, small plans are maintained generally by small employers. Thus, the Department believes that assessing the impact of this final rule on small plans is an appropriate substitute for evaluating the effect on small entities. The definition of small entity considered appropriate for this purpose differs, however, from a definition of small business based on size standards promulgated by the Small Business Administration (SBA)[127] pursuant to the Small Business Act.[128] The Department solicited comments on this assumption in the proposed rule; however, no comments were received.

The Department has determined that this final rule could have a significant impact on a substantial number of small entities during the first year. Therefore, the Department has prepared a Final Regulatory Flexibility Analysis that is presented below.

3.1. Need for and Objectives of the Rule

The Department believes that this final rule is an appropriate way to provide clarity and certainty regarding the application of fiduciary obligations of loyalty and prudence with respect to exercises of shareholder rights, including proxy voting. Despite past efforts to make clear fiduciary obligations in this regard, the Department is concerned that its existing sub-regulatory guidance may have inadvertently created the perception that fiduciaries must vote proxies on every shareholder proposal to fulfill their obligations under ERISA. This belief may have caused some fiduciaries to pursue proxy proposals that have no connection to increasing the value of investments used to pay benefits or defray the reasonable plan administrative expenses.

Both of these concerns point to the risk that a plan's proxy voting activity will sometimes impair rather than advance participants' economic interest in their benefits. This final rule aims to ensure that the costs plans incur to vote proxies and exercise other shareholder rights are economically justified, and that responsible fiduciaries' use of third-party advice supports rather than jeopardizes their adherence to ERISA's fiduciary requirements.

The Department is monitoring other federal agencies whose statutory and regulatory requirements overlap with ERISA. In particular, the Department is monitoring SEC rules and guidance to avoid creating duplicate or overlapping requirements with respect to proxy voting.

3.2. Significant Issues Raised by Public Comments in Response to the IFRA and Changes Made to the Proposed Rule in Response

One of the most significant issue raised by commenters was that paragraphs (e)(3)(i) and (ii) of the proposal require a fiduciary to undertake an economic impact analysis in advance of each issue that is the subject of a proxy vote in order to even consider voting. A commenter further noted that a fiduciary may not discover until after the analysis is performed that the cost involved in determining whether to vote outweighed the economic benefit to the plan. The Department recognizes the concerns expressed regarding potential increased costs and liability exposure associated with these provisions, as well as potential risks to plan investments that could result from fiduciaries not voting when prudent to do so. Therefore, after carefully considering comments, the Department was persuaded to eliminate paragraphs (e)(3)(i) and (ii) and adopt a more principles-based, less prescriptive approach in the final rule that reduces the cost burden associated with the proposed rule. This revision to the proposal is further discussed in Section 3.5 below.

In the proposal, the Department included an illustration to try to capture the cost burden on service providers from the rule. This illustration was based on certain assumptions the Department described as speculative in the proposal, and many of the commenters criticized its basis. In response to the commenters and changes made to the rule since the proposal, the Department has removed this illustration. For a more detailed description about the Department's decision, please refer to the Cost section above.

Some commenters were concerned that the rule would be burdensome on small plan sponsors. One commenter expressed concern that the requirements of the regulation will have a significant impact on small entities because of their limited staff resources. The Department acknowledges this concern as well as the concern that smaller plans may not be able to absorb the additional burden of the regulation as easily as larger plans. As described in the Cost section

[122] The burden is estimated as follows: 63,911 plans * 0.5 hours = 31,955.4 hours for both a plan fiduciary and clerical staff. A labor rate of $134.21 is used for a plan fiduciary and a labor rate of $55.14 for clerical staff (31,955.4 * $134.21 = $4,288,739 and 31,955.4 * $55.14 = $1,762,023).

[123] 5 U.S.C. 601 *et seq.* (1980).

[124] 5 U.S.C. 551 *et seq.* (1946).

[125] 5 U.S.C. 604 (1980).

[126] The Department consulted with the Small Business Administration Office of Advocacy in making this determination, as required by 5 U.S.C. 603(c) and 13 CFR 121.903(c) in a memo dated June 4, 2020.

[127] 13 CFR 121.201 (2011).

[128] 15 U.S.C. 631 *et seq.* (2011).

above, the Department has amended the proposed rule's requirements and adopted a less prescriptive, principles-based approach in the final rule that mirrors and supplements requirements contained in the Department's prior sub-regulatory guidance and industry best practices. These changes will substantially reduce the Department's estimate of the proposed rule's cost impact.

Another commenter expressed concern that the Department substantially underestimated costs for small plans, as many small plans would need to hire a service provider to produce additional documentation to supplement existing investment policy statements. The Department recognizes that plans may need to make various changes to compliance policies and procedures to respond to the rule, so it has added an additional cost for the time it takes to develop or update such policies and procedures in the final rule.

3.2. Affected Small Entities

This final rule will affect ERISA-covered pension, health, and welfare plans that hold stock either through common stock or employer securities. This includes plans that indirectly hold stocks through collective trusts, master trusts, pooled separate accounts, and other similar plan asset investment entities. Plans that only hold their assets in registered investment companies, such as mutual funds, will be unaffected by the final rule.

There is minimal data available about small plans' stock holdings. The primary source of information on assets held by pension plans is the Form 5500. Schedule H, which reports data on stock holdings, is filed almost exclusively by large plans. While the majority of participants and assets are in large plans, most plans are small plans (plans with fewer than 100 participants). It is likely that many small defined benefit plans hold stock. Many small defined contribution plans hold stock only through mutual funds, and consequently would not be affected by this final rule. In 2018, there were 39,142 small defined benefit plans and 590,254 small defined contribution plans. The Department lacks sufficient data to estimate the number of small plans that hold stock, but it assumes that small plans are significantly less likely to hold stock than larger plans. The Department did not receive any comments or additional data from commenters regarding the number of small plans that hold stock directly or indirectly. As discussed elsewhere, while the Department assumes that small affected entities will spend some time familiarizing themselves with the rule, it expects that even in the case of small plans that hold stock directly or indirectly, these costs will be small, because the required activities are reflected in common practice. Therefore, for purposes of determining whether a substantial number of small plans are affected, the Department presumes that five percent of small plans hold stock resulting in as assumed 31,470 affected small plans.

The Department recognizes that service providers, including small service providers who act as asset managers, could also be impacted by this rule, if they provide compliance assistance to the plans they serve. The Department does not have complete information on the number of affected small service providers. However, the Department does not believe that there will be more service providers than the 63,911 affected plans. The Department assumes the number of service providers who will experience a substantial impact from the final rule will be significantly smaller as only about 7.5 percent of service providers in the NAICS categories that could be affected have revenues below $100,000.[129] As discussed in Table 2, below, the Department estimates that compliance costs in the first year are less than $900. Therefore, only service providers with revenues less than $100,000 could experience a cost that is more than one percent of revenues. If service providers incur compliance costs, they could pass some of these costs onto plans and experience a smaller impact.

3.4. Estimate Cost Impact of the Final Rule on Affected Small Entities

This final rule will benefit small plans, by providing guidance regarding how ERISA's fiduciary duties apply to proxy voting and the monitoring of proxy advisory firms, and in particular, when fiduciaries should refrain from voting. Plan fiduciaries will be able to better conserve plan assets by having clear direction to refrain from researching and voting on proposals that they prudently determine have no material effect on the investment performance of the plan's portfolio (or investment performance of assets under management in the case of an investment manager). The final rule also will benefit plans by improving the frequency with which voting resources are expended on matters that the fiduciary has prudently determined are substantially related to the issuer's business activities or are expected to have a material effect on the value of the investment. Cost savings and other benefits to small plans will flow to plan participants and beneficiaries in the form of more secure retirement income.

As discussed under the Costs section above, while the Department assumes that small affected entities will spend some time familiarizing themselves with the rule, it expects that these familiarization costs will be small, because the required activities are reflected in common practice. The Department estimates it will take four hours for an in-house attorney to review the rule, at an hourly labor cost of $138.41,[130] resulting in an average cost of $536.84. The Department believes small plans are likely to rely on service providers to monitor regulatory changes and make necessary changes to the plan, so this is likely an overestimate of the costs incurred by small plans to familiarize themselves with the rule.

Fiduciaries of plans must ensure that all investments are prudently monitored. The final rule provides that fiduciaries responsible for the exercise of shareholder rights must maintain records on proxy voting activities and other exercises of shareholder rights in order to demonstrate compliance with ERISA's fiduciary provisions. The Department assumes that, because the documentation of fiduciary decision-making is a common practice, responsible fiduciaries are likely already recording and maintaining documentation related to their own and investment managers' actions, including voting proxies and exercising other shareholder rights.

The final rule will have a small impact on plans that are not currently in full compliance, because their

[129] To capture the number of potentially affected service providers, the Department looked at the number of small entities with the following North American Industry Classification System (NAICS) Codes: 523110 Investment Banking and Securities Dealing; 523920 Portfolio Management; 523930 Investment Advice; 523991 Trust, Fiduciary, and Custody Activities; and 525910 Open-End Investment Funds. Small entities were identified based on their revenue and the size standards from the SBA. According to data provided by the SBA, the Department estimates there are 8,616 small entities in these industries with revenues less than $100,000. This accounts for 7.5 percent of all firms in these industries. The calculation of the number of firms by industry is based on: NAICS. *Businesses by NAICS, https://www.naics.com/business-lists/counts-by-company-size/.*

[130] Labor costs are based on statistics from *Labor Cost Inputs Used in the Employee Benefits Security Administration, Office of Policy and Research's Regulatory Impact Analyses and Paperwork Reduction Act Burden Calculation,* Employee Benefits Security Administration (June 2019), *www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/technical-appendices/labor-cost-inputs-used-in-ebsa-opr-ria-and-pra-burden-calculations-june-2019.pdf.*

fiduciaries will be required to maintain records or document decisions related to voting proxies or exercising other shareholder rights. Much of the information required to comply with this requirement is generated by affected entities in the normal course of business; however, additional time may be required to maintain the proper documentation. The Department estimates that compliance with this final regulation will require 30 minutes of a plan fiduciary's time and 30 minutes of a clerical worker's time. The Department assumes an hourly rate of $134.21 for a plan fiduciary and an hourly rate of $55.14 for a clerical worker,[131] resulting in an estimated per-entity annual cost of $94.68.[132]

Additionally, the Department estimates that to comply with the rule, many plans will need to either develop or update proxy-voting policies and procedures. This is particularly true for plans choosing to adopt one of the final rule's safe harbors. The Department estimates that it will take two hours for a legal professional to develop or update relevant policies and procedures. The Department assumes an hourly rate of $134.21 for a legal professional, resulting in an estimate per-entity cost of $268.42 in the first year.

Under these assumptions, the Department estimates the additional requirements of the rule will increase costs by $899.94 per plan in the first year and $94.68 per plan in subsequent years, on average. This is illustrated in Table 2 below.

TABLE 2—COSTS FOR PLANS TO COMPLY WITH REQUIREMENTS

Affected entity	Labor rate	Hours	Year 1 cost	Year 2 cost
Documentation: Plan Fiduciary	$134.21	0.5	$67.11	$67.11
Documentation: Clerical workers	55.14	0.5	27.57	27.57
Rule Familiarization: Plan Fiduciary	134.21	4	536.84	0
Develop or Update Proxy-Voting Policies and Procedures	134.21	2	268.42	0
Total			899.94	94.68

Source: DOL calculations based on statistics from *Labor Cost Inputs Used in the Employee Benefits Security Administration, Office of Policy and Research's Regulatory Impact Analyses and Paperwork Reduction Act Burden Calculation,* Employee Benefits Security Administration (June 2019), *www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/technical-appendices/labor-cost-inputs-used-in-ebsa-opr-ria-and-pra-burden-calculations-june-2019.pdf.*

To put these costs in perspective, the Department looked at how the additional cost from the proposed rule would compare to the average total plan cost of 401(k) plans by assets. Plan costs include investment fees as well as administrative and recordkeeping fees. The way plan costs are paid vary by plan. A 2019 survey of 240 plan sponsors found that 33 percent of defined contribution (DC) plans paid all recordkeeping and administrative fees through investment revenue, while 52 percent of DC plans paid recordkeeping and administrative fees through a direct fee.[133] Accounts from the industry purport that per-participant recordkeeping fees are becoming the best practice standard; this trend has been driven by digital recordkeeping technology that requires the same amount of resources for large accounts as small accounts.[134]

Fees paid by plans also vary by firm size. A survey of 361 defined contribution plans for the Investment Company Institute calculated an ''all-in'' fee that included both administrative and investment fees paid by the plan and the participant. They found that small plans with 10 participants pay approximately 50 basis points more than plans with 1,000 participants. Further, small plans with 10 participants are paying about 90 basis points more than large plans with 50,000 participants.[135] Another study documented the same trend, noting that larger plans tend to have lower fees because larger plans tend to have a greater share of assets invested in index funds, which tend to have lower expenses. Additionally, large 401(k) plans are able to spread the fixed costs across more participants, lowering the per participant fee.[136]

For this analysis, the Department relies on data from BrightScope to establish a baseline of total plan fees, before the implementation of this rule. In August of 2020, BrightScope released updated total plan costs based on 2017 data. Their total plan cost includes asset-based investment management fees, asset-based administrative and advice fees, and other fees from the Form 5500 and audited financial statements of ERISA-covered 401(k) plans.[137] This data does not include plans with fewer than 100 participants, the standard set for a small plan in this analysis. However, the Department believes that the median total plan costs, provided by BrightScope, serves as a helpful reference point when considering the additional burden from this rule.

Table 3 shows total plan costs from BrightScope; plan cost information is based on categories of plans with assets less than $1 million, between $1 million and $10 million, and between $10 million and $50 million. The Department provides as the impact of the rule the additional cost plans will incur as a percent of plan assets, using the median asset value of each category, to illustrate how the rule is likely to affect plans with different amounts of assets. As seen in the table below, the estimated burden in the first year will

[131] Labor costs are based on statistics from Labor Cost Inputs Used in the Employee Benefits Security Administration, Office of Policy and Research's Regulatory Impact Analyses and Paperwork Reduction Act Burden Calculation, Employee Benefits Security Administration (June 2019), *www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/technical-appendices/labor-cost-inputs-used-in-ebsa-opr-ria-and-pra-burden-calculations-june-2019.pdf.*

[132] This cost is estimated as: 0.5 hours * $134.21 + 0.5 hours * $55.14 = $94.68.

[133] Deloitte. ''2019 Defined Contribution Benchmarking Survey Report: the Retirement Landscape has Changed—Are Plan Sponsors Ready?'' *www2.deloitte.com/us/en/pages/human-capital/articles/annual-defined-contribution-benchmarking-survey.html.*

[134] Manganaro, John. ''Recordkeeping Fees Under the Microscope Retirement Plans of All Sizes are Seeing Their Recordkeeping Fee Schedules Questioned, Especially When Those Fees are Expressed as a Percentage of Assets.'' Planadviser. (November 2019). *www.planadviser.com/recordkeeping-fees-microscope/.*

[135] Deloitte Consulting and Investment Company Institute, ''Inside the Structure of Defined Contribution/401(k) Plan Fees, 2013: A Study Assessing the Mechanics of the 'All-in' Fee'' (Aug. 2014).

[136] BrightScope, ICI. ''The BrightScope/ICI Defined Contribution Plan Profile: a Close Look at 401(k) Plans, 2017.'' (August 2020).

[137] BrightScope, ICI. ''The BrightScope/ICI Defined Contribution Plan Profile: a Close Look at 401(k) Plans, 2017.'' (August 2020).

increase the costs significantly for small plans with minimal assets. The cost in subsequent years is negligible—less than one percent of plan assets for even the smallest size category and for most plans less than 0.25 percent of plan assets.

TABLE 3—TOTAL FIRST YEAR PLAN COST AS A PERCENT OF PLAN ASSETS FOR PLANS WITH LESS THAN 100 PARTICIPANTS

Plan assets	Number of plans [a]		Beginning median total plan cost [b] (percent)	Additional plan cost from the rule [c]
	Defined benefit	Defined contribution		Percent of mid-point in asset range
$1–24K	12	1,750	1.24 [d]	7.500
$25–49K	8	1,072	1.24 [d]	2.368
$50–99K	37	1,716	1.24 [d]	1.200
$100–249K	188	3,638	1.24 [d]	0.514
$250–499K	300	4,124	1.24 [d]	0.240
$500K–999K	433	5,095	1.24 [d]	0.120
$1 Million to $10 Million	547	6,458	1.05	0.018
$10 Million to $50 Million	202	2,818	0.78	0.003

[a] Calculated as five percent of plans in each asset range, based on data from the 2018 Form 5500 for the distribution of pension plans with fewer than 100 participants by type of plan and plan assets. As the Form 5500 does not allow a determination of which small plans has stock, the actual size distribution is unknown. The population distribution is used.

[b] Total plan cost is BrightScope's measure of the total cost of operating the 401(k) plan and includes asset-based investment management fees, asset-based administrative and advice fees, and other fees (including insurance charges) from the Form 5500 and audited financial statements of ERISA-covered 401(k) plans. Total plan cost is computed only for plans with sufficiently complete information. The sample is 53,856 plans with $4.4 trillion in assets. BrightScope audited 401(k) filings generally include plans with 100 participants or more. Plans with fewer than four investment options or more than 100 investment options are excluded from BrightScope audited 401(k) filings for this analysis. The data does not include DB plans, but due to lack of comparable data it is applied to DB plans as a proxy for their plan costs. *Source:* BrightScope, ICI. ''The BrightScope/ICI Defined Contribution Plan Profile: a Close Look at 401(k) Plans, 2017.'' (August 2020).

[c] The Department estimates that additional plan cost from the rule will be $899.94. The Department applied this fixed cost as a percent of mid-point in each asset range.

[d] BrightScope did not differentiate between plans with less than $1 million in assets; however, as most of the small plans have less than $1 million in assets, the Department applied this broader estimate to smaller sub-sets of assets to illustrate how small plans are likely to affected by the rule.

The Department believes that this is likely an overestimate of the costs faced by small plans, as small plans are likely to rely on service providers. The Department believes these service providers offer economies of scale in meeting the requirements of the final rule; however, the Department does not have data that would allow it to estimate the number of service providers acting in such a capacity for these plans.

The time required to make necessary changes to compliance policies and procedures in response to the rule may vary widely between plans, the Department believes the requirements in the final rule closely resemble existing prior guidance and industry best practices. The Department believes that, on average, the marginal cost to meet the additional requirements regulation, outside of existing fiduciary duties, will be small because the required activities are reflected in common practice and the requirements are similar to prior guidance. Further, plan fiduciaries would be able to conserve plan assets by refraining from researching and voting on proposals that they prudently determine do not have a material effect on the value of the plan's investment. Thus, the final rule would result in cost savings and other benefits for small plan sponsors.

3.5. Steps the Agency Has Taken To Minimize the Significant Economic Impact on Small Entities

As discussed above, the Department's longstanding position is that the fiduciary duties of prudence and loyalty under ERISA sections 404(a)(1)(A) and 404(a)(1)(B) apply to the exercise of shareholder rights, including proxy voting, proxy voting policies and guidelines, and the selection and monitoring of proxy advisory firms. These duties apply to all affected entities–large and small. Accordingly, no special actions were taken into consideration for small entities.

As discussed above, after carefully considering comments, the Department was persuaded to eliminate paragraphs (e)(3)(i) and (ii) and adopt a more principle-based, less prescriptive approach in the final rule that will reduce much of the cost burden associated with the proposed rule. Paragraph (e)(3)(i) of the proposal provided that a plan fiduciary *must* vote any proxy where the fiduciary prudently determined that the matter being voted upon would have an economic impact on the plan after considering those factors described in paragraph (e)(2)(ii) of the proposal and taking into account the costs involved (including the cost of research, if necessary, to determine how to vote). Paragraph (e)(3)(ii) of the proposal provided that a plan fiduciary must *not* vote any proxy unless the fiduciary prudently determined that the matter being voted upon would have an economic impact on the plan after considering those factors described in paragraph (e)(2)(ii) of the proposal and taking into account the costs involved. This is a significant adjustment from the proposal that results in a less prescriptive, more principles-based approach that will reduce much of the cost burden associated with the proposed rule for all plans, including small plans. See the section above entitled ''Elimination of Paragraphs (e)(3)(i) and (ii) from the Proposal'' for a more detailed discussion of this change.

4. Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 [138] requires each federal agency to prepare a written statement assessing the effects of any

[138] 2 U.S.C. 1501 *et seq.* (1995).

federal mandate in a proposed or final agency rule that may result in an expenditure of $100 million or more (adjusted annually for inflation with the base year 1995) in any one year by state, local, and tribal governments, in the aggregate, or by the private sector. For purposes of the Unfunded Mandates Reform Act, as well as Executive Order 12875, this final rule does not include any federal mandate that the Department expects would result in such expenditures by state, local, or tribal governments, or the private sector. This final rule will not result in an expenditure of $100 million or more in any one year, because the Department is simply restating and modernizing fiduciary practices related to voting rights and aligning its regulations to the extent possible with guidance issued by the SEC.

5. Federalism Statement

Executive Order 13132 outlines fundamental principles of federalism and requires federal agencies to adhere to specific criteria when formulating and implementing policies that have ''substantial direct effects'' on the states, the relationship between the national government and states, or on the distribution of power and responsibilities among the various levels of government. Federal agencies promulgating regulations that have federalism implications must consult with state and local officials and describe the extent of their consultation and the nature of the concerns of state and local officials in the preamble to the final rule.

In the Department's view, this final rule does not have federalism implications because it does not have direct effects on the states, the relationship between the national government and the states, or the distribution of power and responsibilities among various levels of government. The final rule describes requirements and permitted practices related to the exercise of shareholder rights under ERISA. While ERISA generally preempts state laws that relate to ERISA plans, and preemption typically requires an examination of the individual law involved, it appears highly unlikely that the provisions in this final regulation would have preemptive effect on general state corporate laws.

Statutory Authority

This regulation is adopted pursuant to the authority in section 505 of ERISA (Pub. L. 93–406, 88 Stat. 894; 29 U.S.C. 1135) and section 102 of Reorganization Plan No. 4 of 1978 (43 FR 47713, October 17, 1978), effective December 31, 1978 (44 FR 1065, January 3, 1979), 3 CFR 1978 Comp. 332, and under Secretary of Labor's Order No. 1–2011, 77 FR 1088 (Jan. 9, 2012).

List of Subjects in 29 CFR Parts 2509 and 2550

Employee benefit plans, Employee Retirement Income Security Act, Exemptions, Fiduciaries, investments, Pensions, Prohibited transactions, Reporting and recordkeeping requirements, Securities.

For the reasons set forth in the preamble, the Department amends parts 2509 and 2550 of subchapters A and F of chapter XXV of title 29 of the Code of Federal Regulations as follows:

Subchapter A—General

PART 2509—INTERPRETIVE BULLETINS RELATING TO THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974

■ 1. The authority citation for part 2509 continues to read as follows:

Authority: 29 U.S.C. 1135. Secretary of Labor's Order 1–2003, 68 FR 5374 (Feb. 3, 2003). Sections 2509.75–10 and 2509.75–2 issued under 29 U.S.C. 1052, 1053, 1054. Sec. 2509.75–5 also issued under 29 U.S.C. 1002. Sec. 2509.95–1 also issued under sec. 625, Pub. L. 109–280, 120 Stat. 780.

§ 2509.2016–01 [Removed]

■ 2. Remove § 2509.2016–01.

Subchapter F—Fiduciary Responsibility Under the Employee Retirement Income Security Act of 1974

PART 2550—RULES AND REGULATIONS FOR FIDUCIARY RESPONSIBILITY

■ 3. The authority citation for part 2550 continues to read as follows:

Authority: 29 U.S.C. 1135 and Secretary of Labor's Order No. 1–2011, 77 FR 1088 (January 9, 2012). Sec. 102, Reorganization Plan No. 4 of 1978, 5 U.S.C. App. at 727 (2012). Sec. 2550.401c–1 also issued under 29 U.S.C. 1101. Sec. 2550.404a–1 also issued under sec. 657, Pub. L. 107–16, 115 Stat 38. Sec. 2550.404a–2 also issued under sec. 657 of Pub. L. 107–16, 115 Stat. 38. Sections 2550.404c–1 and 2550.404c–5 also issued under 29 U.S.C. 1104. Sec. 2550.408b–1 also issued under 29 U.S.C. 1108(b)(1). Sec. 2550.408b–19 also issued under sec. 611, Pub. L. 109–280, 120 Stat. 780, 972. Sec. 2550.412–1 also issued under 29 U.S.C. 1112.

■ 4. Section 2550.404a–1 is amended by adding paragraph (e), revising paragraph (g), and republishing paragraph (h) to read as follows:

§ 2550.404a-1 Investment duties.

* * * * *

(e) *Proxy voting and exercise of shareholder rights.* (1) The fiduciary duty to manage plan assets that are shares of stock includes the management of shareholder rights appurtenant to those shares, such as the right to vote proxies.

(2)(i) When deciding whether to exercise shareholder rights and when exercising such rights, including the voting of proxies, fiduciaries must carry out their duties prudently and solely in the interests of the participants and beneficiaries and for the exclusive purpose of providing benefits to participants and beneficiaries and defraying the reasonable expenses of administering the plan.

(ii) The fiduciary duty to manage shareholder rights appurtenant to shares of stock does not require the voting of every proxy or the exercise of every shareholder right. 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, plan fiduciaries must:

(A) Act solely in accordance with the economic interest of the plan and its participants and beneficiaries;

(B) Consider any 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 promote non-pecuniary benefits or goals unrelated to those financial interests of the plan's participants and beneficiaries;

(D) Evaluate material facts that form the basis for any particular proxy vote or other exercise of shareholder rights;

(E) Maintain records on proxy voting activities and other exercises of shareholder rights; and

(F) Exercise prudence and diligence in the selection and monitoring of persons, if any, selected to advise or otherwise assist with exercises of shareholder rights, such as providing research and analysis, recommendations regarding proxy votes, administrative services with voting proxies, and recordkeeping and reporting services.

(iii) Where the authority to vote proxies or exercise shareholder rights has been delegated to an investment manager pursuant to ERISA section 403(a)(2), or a proxy voting firm or other person who performs advisory services as to the voting of proxies, a responsible plan fiduciary shall prudently monitor the proxy voting activities of such investment manager or proxy advisory firm and determine whether such activities are consistent with paragraphs (e)(2)(i) and (ii) and (e)(3) of this section.

(iv) A fiduciary may not adopt a practice of following the recommendations of a proxy advisory firm or other service provider without a determination that such firm or service provider's proxy voting guidelines are consistent with the fiduciary's obligations described in paragraphs (e)(2)(ii)(A) through (E) of this section.

(3)(i) In deciding whether to vote a proxy pursuant to paragraphs (e)(2)(i) and (ii) of this section, fiduciaries may adopt proxy voting policies providing that the authority to vote a proxy shall be exercised pursuant to specific parameters prudently designed to serve the plan's economic interest. Paragraphs (e)(3)(i)(A) and (B) of this section set forth optional means for satisfying the fiduciary responsibilities under sections 404(a)(1)(A) and 404(a)(1)(B) of ERISA with respect to decisions whether to vote, provided such policies are developed in accordance with a fiduciary's obligations under ERISA as set forth in the applicable provisions of paragraphs (e)(2)(i) and (ii) of this section. Paragraphs (e)(3)(i)(A) and (B) of this section do not establish minimum requirements or the exclusive means for satisfying these responsibilities. A plan may adopt either or both of the following policies:

(A) A policy to limit voting resources to particular types of proposals that the fiduciary has prudently determined are substantially related to the issuer's business activities or are expected to have a material effect on the value of the investment.

(B) A policy of refraining from voting on proposals or particular types of proposals when the plan's holding in a single issuer relative to the plan's total investment assets is below a quantitative threshold that the fiduciary prudently determines, considering its percentage ownership of the issuer and other relevant factors, is sufficiently small that the matter being voted upon is not expected to have a material effect on the investment performance of the plan's portfolio (or investment performance of assets under management in the case of an investment manager).

(ii) Plan fiduciaries shall periodically review proxy voting policies adopted pursuant to paragraph (e)(3)(i) of this section.

(iii) No proxy voting policies adopted pursuant to paragraph (e)(3)(i) of this section shall preclude submitting a proxy vote when the fiduciary prudently determines that the matter being voted upon is expected to have a material effect on the value of the investment or the investment performance of the plan's portfolio (or investment performance of assets under management in the case of an investment manager) after taking into account the costs involved, or refraining from voting when the fiduciary prudently determines that the matter being voted upon is not expected to have such a material effect after taking into account the costs involved.

(4)(i)(A) The responsibility for exercising shareholder rights lies exclusively with the plan trustee except to the extent that either:

(*1*) The trustee is subject to the directions of a named fiduciary pursuant to ERISA section 403(a)(1); or

(*2*) The power to manage, acquire, or dispose of the relevant assets has been delegated by a named fiduciary to one or more investment managers pursuant to ERISA section 403(a)(2).

(B) Where the authority to manage plan assets has been delegated to an investment manager pursuant to section 403(a)(2), the investment manager has exclusive authority to vote proxies or exercise other shareholder rights appurtenant to such plan assets in accordance with this section, except to the extent the plan, trust document, or investment management agreement expressly provides that the responsible named fiduciary has reserved to itself (or to another named fiduciary so authorized by the plan document) the right to direct a plan trustee regarding the exercise or management of some or all of such shareholder rights.

(ii) 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 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 statement, 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.

(5) This section does not apply to voting, tender, and similar rights with respect to such securities that are passed through pursuant to the terms of an individual account plan to participants and beneficiaries with accounts holding such securities.

* * * * *

(g) *Applicability date.* (1) Except for paragraph (e) of this section, this section shall apply in its entirety to all investments made and investment courses of action taken after January 12, 2021.

(2) Plans shall have until April 30, 2022, to make any changes to qualified default investment alternatives described in § 2550.404c–5, where necessary to comply with the requirements of paragraph (d)(2) of this section.

(3) Paragraph (e) of this section applies on January 15, 2021. Fiduciaries, other than investment advisers subject to 17 CFR 275.206(4)–6, shall have until January 31, 2022, to comply with the requirements of paragraphs (e)(2)(ii)(D) and (E) of this section. All fiduciaries shall have until January 31, 2022 to comply with the requirements of paragraphs (e)(2)(iv) and (e)(4)(ii) of this section.

(h) *Severability.* If any provision of this section is held to be invalid or unenforceable by its terms, or as applied to any person or circumstance, or stayed pending further agency action, the provision shall be construed so as to continue to give the maximum effect to the provision permitted by law, unless such holding shall be one of invalidity or unenforceability, in which event the provision shall be severable from this section and shall not affect the remainder thereof.

Signed at Washington, DC.

Jeanne Klinefelter Wilson,

Acting Assistant Secretary, Employee Benefits Security Administration, Department of Labor.

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