



March 27, 2023

# Department of Labor Guidance and Regulations on the Exercise of Shareholder Rights by Private-Sector Pension Plans

## Introduction

The fiduciary standards in the Employee Retirement Income Security Act of 1974 (ERISA; P.L. 93-406, as amended) require that individuals who make decisions for private-sector pension plans (referred to as *fiduciaries*) adhere to specified standards of conduct. The standards include an obligation to act prudently and solely for the exclusive purpose of providing benefits to participants and beneficiaries and for defraying reasonable expenses. Among those who are fiduciaries are individuals who choose and manage plan investments. The standards apply to *defined benefit* plans, in which retirees usually receive monthly payments (sometimes referred to as *traditional* pensions), and *defined contribution* plans, in which participants have individual accounts (e.g., 401(k) plans).

Among other responsibilities, pension plan fiduciaries must manage plan assets that involve shares of corporate stock and, thus, may be required to make and monitor decisions about voting proxies and exercising shareholder rights. The Department of Labor (DOL) has published guidance over the past few decades outlining these responsibilities.

## Proxy Voting and Exercising Shareholder Rights

Pension plans typically hold stocks as part of their investment portfolios. Ownership of a company's stock confers partial ownership and grants the investor certain rights. One of these rights may include the right to vote on matters such as electing the board of directors and the approval of mergers and acquisitions. Shareholders can exercise their vote in person. However, most shareholders do not attend corporate annual meetings. Typically, shareholders have the right to appoint proxies. A proxy is a written authorization that delegates the shareholder's voting power to another person or, more typically, an institution.

DOL's long-standing position is that plan fiduciaries should engage in proxy voting activities in discharging their fiduciary obligation to prudently manage plan investments. A pension plan fiduciary is subject to fiduciary responsibility when deciding whether to vote or not to vote (via proxy or in person) and when deciding how to vote. The details of how fiduciaries determine whether and how to vote have been the subject of various regulations.

Due to the large number and diverse array of issues that shareholders may vote on, institutional investors, such as mutual funds and pension plans, frequently use proxy advisory firms for proposal voting recommendations. Proxy advisory firms provide institutional investors with research and recommendations on management and shareholder proposals that are voted on at annual corporate meetings.

Two firms—Institutional Shareholder Services (ISS) and Glass Lewis—control much of the proxy advisory business. Pension plan fiduciaries are subject to fiduciary responsibility in the selection and monitoring of proxy advisory firms and ensuring that any proxy advisory firm votes in the best interest of plan participants.

## Concerns About Voting and Fiduciary Obligations

A pension plan's fiduciary obligations include voting in a manner that reflects the duty to act solely in the interest of plan participants and beneficiaries. Recent discussions focus on which factors are financially relevant to a corporation and, thus, a pension plan's investment performance—and whether and how proposals related to these factors should be voted on by institutional investors. For example, are fiduciaries expressing their personal preferences or considering what they believe are important financial factors when they support proposals to require companies to disclose their greenhouse gas emissions? Another discussion is whether proxy advisory firms might have conflicts of interest (such as making recommendations on shareholder proposals while also providing consulting services to those same firms).

## Earlier DOL Guidance

In a 1988 opinion letter to Avon Products, Inc., DOL took the position that “the fiduciary act of managing plan assets that are shares of corporate stock includes the voting of proxies appurtenant to those shares” and that a pension plan fiduciary “has a duty to monitor decisions made and actions taken by investment managers with regard to proxy voting.”

In 1994, 2008, and 2016, DOL issued non-regulatory guidance in the form of Interpretive Bulletins (IBs), and in 2018, in the form of a Field Assistance Bulletin (FAB), concerning fiduciary duties when exercising shareholder rights:

- DOL, in IB 94-2, recognized that fiduciaries may engage in shareholder activities if—after accounting for costs—such activities are expected to enhance the value of the plan's investment. DOL reiterated that fiduciaries are not permitted to subordinate the economic interests of participants to unrelated objectives.
- DOL, in IB 2008-02, clarified that fiduciaries voting proxies, after taking into account costs associated with exercising shareholder rights, “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.”

- Later, IB 2016-01 reinstated IB 94-2 with some modifications, noting that IB 2008-02 “worked to discourage ERISA plan fiduciaries who are responsible for the management of shares of corporate stock from voting proxies and engaging in other prudent exercises of shareholder rights.” In IB 2016-01, DOL stated that a plan’s investment policy that “contemplates engaging in shareholder activities that are intended to monitor or influence the management of corporations can be consistent with a fiduciary’s duties under ERISA,” provided the activity is likely to enhance the value of the plan’s investment.
- Later, FAB 2018-01 stated that fiduciaries that engage in activities to influence corporate policy might warrant “a documented analysis of the cost of the shareholder activity compared to the expected economic benefit (gain) over an appropriate investment horizon.”

### December 2020 Regulation

On December 16, 2020, under the Trump Administration, DOL issued a final rule relating to the application of ERISA’s prudence and exclusive purpose duties to the exercise of shareholder rights. The regulation stated that fiduciaries were not required to vote all proxies, and proxies must be voted—after taking into account associated costs—with the economic interests of plans and plan participants and in a manner that did not subordinate their interests to any non-economic (what the regulation called *non-pecuniary*) objectives or promote goals unrelated to financial interests of participants and beneficiaries. The regulation included two safe harbors that permitted fiduciaries to limit or refrain from voting in certain situations. In addition, the regulation stated that fiduciaries who delegated proxy voting authority to investment managers or proxy voting firms had to monitor and maintain records on the proxy voting activities and other exercises of shareholder rights.

On March 10, 2021, under the Biden Administration, DOL announced that it would not enforce the December 2020 final rule or pursue enforcement actions and that it intended to revisit the rule in the future.

### December 2022 Regulation

On December 1, 2022, under the Biden Administration, DOL issued a final rule that addressed proxy voting and the exercise of shareholder rights (and the application of fiduciary duty when selecting plan investments, discussed in CRS In Focus IF12328, *Department of Labor Guidance and Regulations on Selecting Private-Sector Pension Plan Investments*). The final rule became effective on January 30, 2023 (with some exceptions). Among other things, DOL noted that the final rule removed from the previous regulation:

- language stating that fiduciaries are not required to vote all proxies,
- two safe harbor provisions that permitted fiduciaries to (1) limit proxy voting resources to proposals that the fiduciary had determined “were substantially related to the issuer’s business activities or were expected to have a material effect on the value of the investment” and (2)

refrain from voting on proposals when the plan’s holding in a single issuer relative to the plan’s total investment assets was below a quantitative threshold,

- the specific monitoring obligations for the use of investment managers or proxy voting firms (noting that monitoring obligations are included more generally elsewhere in the regulation), and
- the requirement to maintain records on proxy voting activities and other exercises of shareholder rights.

In the final rule, DOL stated that the purpose was to clarify the application of ERISA’s fiduciary duties on the exercise of shareholder rights, noting that the 2020 final rule had a “negative impact on plans’ financial performance as they shy away from proxy votes and shareholder engagement activities that are economically relevant.”

### Response to DOL December 2022 Regulation

On January 26, 2023, a coalition of 25 states filed suit to block the rule, saying that DOL overstepped its authority under ERISA to issue the rule.

In the 118<sup>th</sup> Congress, H.J.Res. 30, which would use the Congressional Review Act (CRA; enacted in P.L. 104-121) to nullify the 2022 regulation, was passed by the House and Senate and vetoed by President Biden on March 20, 2023. The House failed to override the veto.

### For More Information

Employee Benefits Security Administration (EBSA), “Interpretive Bulletin Relating to the Employee Retirement Income Security Act of 1974,” 59 *Federal Register* 38860, July 29, 1994, <https://www.federalregister.gov/d/94-18198>.

EBSA, “Interpretive Bulletin Relating to Exercise of Shareholder Rights,” 73 *Federal Register* 61731, October 17, 2008, <https://www.federalregister.gov/d/E8-24552>.

EBSA, “Interpretive Bulletin Relating to the Exercise of Shareholder Rights and Written Statements of Investment Policy, Including Proxy Voting Policies or Guidelines,” 81 *Federal Register* 95879, December 29, 2016, <https://www.federalregister.gov/d/2016-31515>.

EBSA, “Field Assistance Bulletin No. 2018-01,” April 23, 2018, <https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2018-01>.

EBSA, “Fiduciary Duties Regarding Proxy Voting and Shareholder Rights,” 85 *Federal Register* 81658, December 16, 2020, <https://www.govinfo.gov/app/details/FR-2020-12-16/2020-27465>.

EBSA, “Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights,” 87 *Federal Register* 73822-73886, December 1, 2022, <https://www.govinfo.gov/content/pkg/FR-2022-12-01/pdf/2022-25783.pdf>.

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