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New Guidance on Proxy Voting and Investment Policies for Employee Benefit Plans

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The Employee Benefits Security Administration (“EBSA”) recently issued a new Interpretive Bulletin on the legal standards under the Employee Retirement Income Security Act (“ERISA”) that apply to fiduciaries who exercise proxy voting rights and their compliance with investment policies. ERISA generally requires plan fiduciaries to act for the exclusive purpose of providing benefits to participants and beneficiaries and to act prudently. These obligations directly affect employers who are the legal plan administrators or those appointed by the employer to act as fiduciaries (such as an administrative committee) including investment managers. Employers need to be aware of these obligations as they establish and administer their employee benefit plans.

Proxy Voting

The responsibility for voting proxies (or not voting proxies) is generally that of the plan’s trustee. However, such obligation may be made subject to the direction of the named fiduciary or delegated to an investment manager. Particularly with institutional trustees, the trustee will serve ordinarily in a nondiscretionary capacity such that the named fiduciary (usually the company as the plan administrator) remains essentially responsible for proxy voting. In more traditional pension plans, these obligations may be delegated to a dedicated investment manager, subject to the terms of the investment management arrangement.

Generally, proxy votes must be cast on issues that may affect the economic value of the plan’s investments, and the votes may take into account only the plan’s economic interests—not the interests of the employer itself or other unrelated interests. However, EBSA recognizes that fiduciaries must also determine whether the value of exercising these rights outweighs the associated costs including the cost of research, if necessary, to determine how to vote. In certain cases, therefore, the fiduciary may be able to document that the value of exercising the proxy outweighs the costs; in such case, it would be advisable to document that this is the case. Absent such cost considerations, the fiduciary must generally vote the proxy in the interest of the plan. Although it may often be the case that the vote (except in very large plans) will not determine the outcome, the duty to vote the proxy remains a fiduciary obligation.

Investment Policy Statement

Although investment policy statements are not required by ERISA, EBSA notes that the maintenance of such a policy is consistent with ERISA’s fiduciary obligations. Generally, an investment policy statement sets forth guidelines, or general instructions, concerning various types of investment management decisions, which may include proxy voting decisions. However, proxy voting guidelines can be contained in a separate procedure.

Investment policy statements are considered “documents and instruments governing the plan” under Section 404(a)(1)(D) of ERISA. Therefore, the fiduciary (trustee, investment manager, plan administrator, or other

fiduciary, as applicable) would be required to comply with the policy, provided such policy otherwise satisfies the fiduciary obligations under ERISA. Maintenance of an investment policy does not relieve the named fiduciary of its other fiduciary obligations. Therefore, for example, a named fiduciary still must periodically monitor an investment manager's management of plan assets including proper documentation of the investment manager's activities and the named fiduciary's activities in monitoring the investment manager's activities.

Shareholder Activism

EBSA has added to its prior guidance in allowing an investment policy to consider shareholder activism, subject to certain conditions. A plan's investment policy to engage in activities, such as correspondence with corporate management and the exercise of their rights as shareholders, that are intended to monitor or influence the management of corporations in which the plan owns stock, may be consistent with a fiduciary's ERISA obligations. However, the fiduciary must conclude that there is a reasonable expectation that the activity will enhance the economic value of the plan's investment taking into account the costs involved. This might be the case, for example, where plan investments are held as long-term investments or where a plan may not be able to easily dispose of the investment. These activities would generally concern such issues as the independence and expertise of candidates for the corporation's board of directors; assurance that the board has sufficient information to carry out its responsibility to monitor management; the appropriateness of executive compensation; the corporation's policy regarding mergers and acquisitions; the extent of debt financing and capitalization; the nature of long-term business plans; the corporation's investment in training to develop the work force; and other workplace practices and financial and non-financial measures of corporate performance that are reasonably likely to affect the economic value of the plan. However, EBSA cautions that plan fiduciaries risk violating the exclusive purpose rule and the prudence requirements under ERISA when they exercise their fiduciary authority through the proxy process in an attempt to further legislative, regulatory, or public policy issues that have no connection to enhancing the economic value of the plan's investment in the corporation.

Pooled Investments

Pooled investments may sometimes result in conflicting obligations for investment managers. In the event of a conflict between different plans, the Bulletin provides that the investment manager would have to disregard a plan's policy that would be imprudent or not solely in the economic interests of all plan participants. However, if the investment manager reasonably concludes that the application of each plan's voting policy is consistent with ERISA's obligations, to the extent permitted by applicable law, the investment manager must vote the proxies in proportion to each plan's interest in the pooled investment vehicle. As is often the case, an investment manager may 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.

If you have any questions about the new Bulletin, please contact one of the [Employee Benefits and Executive Compensation](#) attorneys at Boulton, Cummings, Conners & Berry PLC:

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