

# U-Turn: Comments on Proxy Voting Advice



Commissioner Hester M. Peirce

July 13, 2022

Thank you, Mr. Chair. I appreciate the staff's diligence, graciousness, professionalism, and hard work throughout this rulemaking process. Staff's valuable time, however, could have been put to better use. For example, staff could have worked immediately on addressing outstanding issues around proxy plumbing and, in several years, on conducting a retrospective review of the 2020 Rules.<sup>[1]</sup> Instead, the request made of the staff was a difficult and pointless one—find a way to redo a freshly adopted rule without any new information to suggest that such a rewrite is warranted. I am sorry that I cannot support the resulting rule.<sup>[2]</sup>

When the Commission proposed these latest amendments nine months ago (the “Redo Proposal”),<sup>[3]</sup> nothing had changed since we adopted our 2020 Rules to justify repeal, so I voted no.<sup>[4]</sup> The feedback we received during this proposal's brief comment period confirmed my initial view.<sup>[5]</sup> As one of many commenters who were baffled by the “regulatory whiplash”<sup>[6]</sup> put it:

*We find it difficult to understand the Commission's decision to propose amending the proxy solicitation exemption qualification requirements prior to having any data on their actual impact or cost. . . . It is not possible to conduct an economic or cost benefit analysis for a rule that has not gone into effect, and the decision to amend a finalized rule without such data may have the unintended consequence of establishing an undesirable precedent impacting regulatory stability going forward.*<sup>[7]</sup>

## I. Rules of the Road

Proxy advisors play a very important role in our markets. By providing research and voting recommendations, they assist investment advisers and institutional investors in making voting decisions about matters relating to the companies in which they invest. Proxy advisors, through the operation of sophisticated electronic voting platforms, also help their clients navigate the logistically challenging voting process. If a client wants, the proxy advisor will pre-populate the client's voting cards with voting recommendations and automatically submit the votes on behalf of the client.

While these offerings are user-friendly, they have potential pitfalls. Investment advisers who use these platforms have a fiduciary duty to exercise their voting authority in the best interest of their clients.<sup>[8]</sup> Although advisers can get help, they cannot outsource that responsibility to anyone, including proxy advisors. Moreover, given the widespread reliance on proxy advisors, automatic voting can have an outsized effect on vote outcomes at public companies. In short, proxy voting advice can be “market moving.”<sup>[9]</sup>

Our 2020 Rules recognized the ability of proxy advisors to move client voting decisions and markets. The rules introduced some procedural protections around the provision of proxy advice, including “engagement policies,” which were intended to ensure that proxy advisor's clients receive transparent, accurate, and complete information on which to make their voting decisions.<sup>[10]</sup> The Commission did not preclude proxy advisors from

offering automatic voting features. Instead, it adopted guidance for investment advisers on how they can use such features consistent with their fiduciary duty (the “Robo-Voting Guidance”).<sup>[11]</sup>

## II. Off-Roaded

Today, we are dumping most of the protections embodied in the 2020 Rules and all of those in the Robo-Voting Guidance, which will be entirely repealed.<sup>[12]</sup> As expressed in the Redo Proposal, the rationale for the Commission’s change of heart—in addition to continued opposition by critics of the 2020 Rules—is that proxy advisors have engaged in a self-improvement campaign and miraculously have acquired the “market-based incentives” that were missing when the Commission adopted its 2020 Rules.<sup>[13]</sup>

Many commenters identified serious flaws in the Commission’s stated rationale, including:

- Given the concentration in the proxy voting advice market, proxy advisors have limited incentives to engage with public companies, particularly smaller ones, to correct errors.<sup>[14]</sup> Moreover, proxy advisors’ amending their own research reports and changing their voting recommendations to correct earlier errors can be costly and bring reputational risk.<sup>[15]</sup>
- The Commission should not assume that proxy advisors’ current voluntary engagement practices, even if they are good, will continue. In fact, since the adoption of the 2020 Rules, one of the largest proxy advisors has trended toward engaging *less* often with issuers.<sup>[16]</sup>
- One commenter provided a study identifying the potential persistence of errors in proxy advice.<sup>[17]</sup> The adopting release optimistically views the study as evidence “that registrants were able to identify those issues and respond using pre-existing mechanisms.”<sup>[18]</sup> Whether anyone saw those responses prior to voting is another question. As one commenter pointed out, even if errors are rare, it is in everyone’s best interest if “companies on the receiving end of a proxy firm’s recommendations have an opportunity to respond to inaccurate or arguably misinterpreted data.”<sup>[19]</sup>

The Commission received letters in support of the Redo Proposal as well. These letters did not include new information to justify the Commission’s U-Turn. Instead, they reiterated concerns that commenters had raised during the prior rulemaking process. The Commission, responding to these concerns, adopted a tailored regulatory framework for proxy voting advice in its 2020 Rules.<sup>[20]</sup> The dearth of new evidence to support the Redo Proposal was not surprising given that the 2020 Rules addressing the application of the proxy rules to proxy voting advice businesses were on ice; last summer, staff publicly announced its intent not to recommend enforcement actions based on the 2020 Rules.<sup>[21]</sup>

## III. Turning Back

Despite the weight of the comments received over the past few months favoring the Commission leaving intact its 2020 work,<sup>[22]</sup> we are undertaking this unnecessary PVAB Rehab—gutting the rules so that little of what we adopted less than two years ago remains. Sadly, the one piece of the existing rules I would have liked to change—the term Proxy Voting Advice Business, or “PVAB”—remains unscathed in the rewrite. We are forging ahead to adopt this recommendation as proposed—as if we had never heard commenters’ concerns about the redo. In essence, the Commission, having pre-populated its voting card nine months ago, did not have much interest in the responses we received during the unnecessarily short comment period.<sup>[23]</sup>

Changing course so dramatically with so little justification does not bode well for the Commission. What credibility will we have as an independent agency if our regulations so drastically swerve from one year to the next? If we keep making U-turns like this one, people might start to wonder whether the GPS we are using is calibrated to respond to political rather than market signals.

Thank you.

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<sup>[1]</sup> Exemptions from the Proxy Rules for Proxy Voting Advice, Exchange Act Release No. 34-89372, 85 Fed. Reg. 55082 (Sept. 3, 2020) [hereinafter “2020 Rules”] (adopting final rules for proxy voting advice businesses).

[2] See Proxy Voting Advice, Exchange Act Release No. 34-95266 (July 13, 2022), <https://www.sec.gov/rules/final/2022/34-95266.pdf> [hereinafter “Adopting Release”].

[3] See Proxy Voting Advice, Exchange Act Release No. 34-93595, 86 Fed. Reg. 67383 (Nov. 26, 2021) [hereinafter “Redo Proposal”].

[4] See Hester M. Peirce, Commissioner, SEC, Dissenting Statement on Proxy Voting Advice Proposal (Nov. 17, 2021), <https://www.sec.gov/news/statement/peirce-proxy-advice-20211117>.

[5] A majority of the comment letters received on the Redo Proposal were not supportive. *Compare* Adopting Release, *supra* note 2, at n.65 (citing a list of critics of the proposed rule), with n.40 (citing a list of supporting commenters). See also Comments on Proposed Rule: Proxy Voting Advice, SEC (Nov. 20, 2021), <https://www.sec.gov/comments/s7-17-21/s71721.htm>.

[6] Letter from John Endean, President, American Business Conference to Vanessa Countryman, Secretary, SEC (Dec. 23, 2021) at 3 (<https://www.sec.gov/comments/s7-17-21/s71721-20110745-264610.pdf>).

[7] Letter from Ani Huang, President and CEO, Center on Executive Compensation to Vanessa Countryman, Secretary, SEC (Dec. 23, 2021) at 1-2 (<https://www.sec.gov/comments/s7-17-21/s71721-20110717-264594.pdf>). See also Letter from the American Securities Association, et al. to Vanessa Countryman, Secretary, SEC (Dec. 23, 2021) at 2 (<https://www.sec.gov/comments/s7-17-21/s71721-20110263-264518.pdf>) (“the SEC decided to reverse the 2020 Reforms *prior to the reforms even going into effect*. It is impossible for the SEC to objectively judge the impact the reforms would have had in practice given the most significant provisions apply beginning with the 2022 proxy season.”).

[8] Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, Investment Company Act Release No. IA-5325, 84 Fed. Reg. 47420, 47421 (Sept. 10, 2019) [hereinafter “Commission Guidance on Proxy Voting Responsibilities”] (“[F]or an investment adviser to form a reasonable belief that its voting determinations are in the best interest of the client, it should conduct an investigation reasonably designed to ensure that the voting determination is not based on materially inaccurate or incomplete information.”).

[9] See 2020 Rules, *supra* note 1, at n.18 and associated text.

[10] Specifically, the rules granted an exemption for proxy advisors to the proxy solicitation rules, to the extent the proxy advisors: (1) prominently disclose material conflicts of interest to their clients along with any policies and procedures regarding how the firm addresses such conflicts and (2) have written policies and procedures reasonably designed to ensure that (i) companies that are the subject of the proxy advisors’ voting advice have such advice made available to them at or prior to the time such advice is provided to proxy advisory clients, and (ii) proxy advisors’ clients have a mechanism by which they can reasonably be expected to become aware of any written statements from those companies. See 17 C.F.R. § 240.14a-2(b)(9) (2021).

[11] Supplement to Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, Investment Advisers Act Release No. IA-5547, 85 Fed. Reg. 55155 (Sept. 3, 2020) [hereinafter “Robo-Voting Guidance”].

[12] See Adopting Release, *supra* note 2, at 41.

[13] See Redo Proposal, *supra* note 3, at 67386-88.

[14] See, e.g., Letter from Carlo Passeri, Senior Director of Capital Markets and Financial Services Policy, Biotechnology Innovation Organization to Vanessa Countryman, Secretary, SEC (Dec. 23, 2021) at 1-2 (<https://www.sec.gov/comments/s7-17-21/s71721-20110739-264606.pdf>); Letter from Benjamin Zycher, Senior Fellow, American Enterprise Institute to the SEC (Oct. 14, 2021) at 3 (<https://www.sec.gov/comments/s7-17-21/s71721-20110748-264612.pdf>); Letter from Tom Quaadman, Executive Vice President, Center for Capital Markets Competitiveness, U.S. Chamber of Commerce to Vanessa Countryman, Secretary, SEC (Dec. 23, 2021) at 4 (<https://www.sec.gov/comments/s7-17-21/s71721-20110258-264516.pdf>).

[15] See e.g., Huang, *supra* note 7, at 7-8.

[16] See Quaadman, *supra* note 14; Huang, *supra* note 7; Letter from John A. Zecca, Executive Vice President, Chief Legal and Regulatory Officer, Nasdaq, Inc. to Vanessa Countryman, Secretary, SEC (Dec. 27, 2021) (<https://www.sec.gov/comments/s7-17-21/s71721-20110818-264663.pdf>); Letter from Ted Allen, Vice President, Policy & Advocacy, Society for Corporate Governance and Darla Stuckey, President and CEO, Society for Corporate Governance to Vanessa A. Countryman, Secretary, SEC (Dec. 30, 2021) (<https://www.sec.gov/comments/s7-17-21/s71721-20111068-264733.pdf>). See also ISS, *FAQs regarding ISS Proxy Research*, ISS Governance, <https://www.issgovernance.com/contact/faqs-engagement-on-proxy-research/#1574276867038-b204d1c3-a920> (last visited July 12, 2022) (“In the US, as from January 2021, drafts are no longer provided to U.S. companies including those in the S&P 500 index.”). The Adopting Release takes comfort in the fact that “ISS continues to allow any registrant to request a copy of its proxy voting advice issued under its Benchmark policy guidelines free of charge after ISS has disseminated the advice to its clients.” Adopting Release, *supra* note 1, at n.142. See ISS, *FAQs regarding ISS Proxy Research*, ISS Governance, <https://www.issgovernance.com/contact/faqs-engagement-on-proxy-research/#1574276741161-7ca718d3-32ae> (last visited July 12, 2022). The rule the Commission is adopting today is agnostic about whether that practice continues.

[17] Letter from Kyle Isakower, Senior Vice President of Regulatory and Energy Policy, The American Council on Capital Formation to Vanessa Countryman, Secretary, SEC (Dec. 22, 2021) (<https://www.sec.gov/comments/s7-17-21/s71721-20110241-264511.pdf>) (detailing the findings of a study in which there were 50 instances where proxy advisors have formulated recommendations based on data or analysis disputed by the companies themselves, an increase from the 42 instances detailed in a 2020 analysis).

[18] Adopting Release, *supra* note 2, at 33.

[19] Letter from Michelle Nellenbach, Vice President of Strategic Initiatives, Bipartisan Policy Center to Vanessa Countryman, Secretary, SEC (Dec. 27, 2021) at 5 (<https://www.sec.gov/comments/s7-17-21/s71721-20111188-264840.pdf>).

[20] See 2020 Rules, *supra* note 1. The 2020 Rules were based primarily on feedback from the Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice, Exchange Act Release No. 34-87457, 84 Fed. Reg. 66518 (Dec. 4, 2019) [hereinafter, “2019 Proposed Rules”] (addressing obligations of those businesses that provide proxy voting advice, including to investment advisers). Additional sources of comment were also considered in the 2020 Rules, including: Comments on Statement Announcing SEC Staff Roundtable on the Proxy Process, SEC (Nov. 15, 2018), <https://www.sec.gov/comments/4-725/4-725.htm>; Comments on Proxy Voting Roundtable, SEC (Feb. 19, 2015), <https://www.sec.gov/comments/4-681/4-681.shtml>; Comments on Proxy Advisory Firm Roundtable, SEC (Dec. 5, 2013), <https://www.sec.gov/comments/4-670/4-670.shtml>; Comments on Concept Release on the U.S. Proxy System, SEC (July 14, 2010), <https://www.sec.gov/comments/s7-14-10/s71410.shtml>.

[21] See Division of Corporation Finance, *Statement on Compliance with the Commission’s 2019 Interpretation and Guidance Regarding the Applicability of the Proxy Rules to Proxy Voting Advice and Amended Rules 14a-1(1), 14a-2(b), 14a-9*, SEC (June 1, 2021), <https://www.sec.gov/news/public-statement/corp-fin-proxy-rules-2021-06-01> (“At the direction of the Chair, we are now considering whether to recommend that the Commission revisit the 2019 Interpretation and Guidance and the 2020 Rule Amendments. In light of this direction, the Division of Corporation Finance has determined that it will not recommend enforcement action to the Commission based on the 2019 Interpretation and Guidance or the 2020 Rule Amendments during the period in which the Commission is considering further regulatory action in this area.”). See also Gary Gensler, Chair, SEC, Statement on the application of the proxy rules to proxy voting advice (June 1, 2021), <https://www.sec.gov/news/public-statement/gensler-proxy-2021-06-01>; Hester M. Peirce, Commissioner, SEC and Elad L. Roisman, Commissioner, SEC, Response to Chair Gensler’s and the Division of Corporation Finance’s Statements Regarding the Application of the Proxy Rules to Proxy Voting Advice (June 1, 2021), <https://www.sec.gov/news/public-statement/peirce-roisman-response-statements-application-proxy-rules-060121>.

[22] See *supra* note 5.

[23] See, e.g., Letter from J.W. Verret, Professor, George Mason University Antonin Scalia Law School to Vanessa Countryman, Secretary, SEC (Dec. 21, 2021) at 12 (<https://www.sec.gov/comments/s7-17-21/s71721-20110192-264452.pdf>) (arguing that comment period should have matched comment period for 2020 rules)