Statement on N-PX Proposal

Commissioner Caroline A. Crenshaw

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Each year, shareholders of corporations are asked to vote on a variety of matters that can influence consequential corporate decisions, including, for example, votes on board composition or executive compensation. Some of the largest shareholders with the most influence over voting are registered investment companies ("funds"), including mutual funds and ETFs.[1] Almost half of U.S. households invest their savings in these funds. [2] Investors rely on these funds not only to help them save, but also to vote on those consequential corporate decisions. Given the enormous responsibility funds have undertaken on behalf of investors, investors should be able to understand how their money is being voted.[3] Yet, this information is not easily accessible to them.[4]

In 2003, the Commission required funds to report annually certain details about how they voted companies' shares on Form N-PX. [5] While this was a good first step, recent academic work has shown that, in its current form, it's too difficult for many investors to find decision useful information in N-PX reports. [6] Accordingly, investors are still largely in the dark when it comes to how the funds they own are voting their money.

Today's proposal is thoughtfully designed to address many of the gaps under the existing reporting regime. In addition to requiring certain institutional investors to report their votes on executive compensation ("Say on Pay") matters, the proposed amendments also would standardize the order in which reporting persons disclose existing information, categorize votes, structure and tag the data reported, and make the description of proxy voting issues consistent across multiple filings. This consistency is fundamental to investors' ability, and perhaps will incentivize investors, to assess how their money is voted.[7] In addition, because all funds will be required to follow the same rules of the road, investors will be able to compare and evaluate voting decisions across the entire market of funds vying for their investing dollars. When shareholders have readily available information about how funds vote their interests, they can hold them to account, which, in turn, could enhance corporate decision making.[8]

I look forward to reading comments on all aspects of this proposal and, as always, I appreciate the views of my colleagues and the hard work and thoughtfulness of the staff.

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[1] Registered investment companies own around 30 percent of U.S. corporate equities and in some cases funds hold a larger percent of a single company's stock. *See* ICI 2021 Fact Book, at figure 2.7 (stating that mutual funds and other registered investment companies held 30 percent of U.S. corporate equities as of year-end 2020).

[2] *Id.* at figure 2.7 (stating that 45.7 percent of U.S. households owned funds in 2020).

[3] *See* Robert J. Jackson, Commissioner, Sec. & Exch. Comm'n, Common Ownership: The Investor Protection Challenge of the 21st Century, Testimony Before the Federal Trade Commission Hearing on Competition and Consumer Protection (Dec. 6, 2018).

[4] N-PX reports can be overwhelmingly long, spanning hundreds of pages. *See* Enhanced Reporting of Proxy Votes by Registered Management Investment Companies; Reporting of Executive Compensation Votes by Institutional Investment Managers, Release Nos. 34-93169 (Sept. 29, 2021) at 10-12. For example, based on staff analysis of reports on Form N-PX, larger funds can have filings in excess of 1,000 pages. *See id*. These reports also can be organized and presented in ways that vary significantly. For example, funds may provide unclear and inconsistent descriptions of voting matters (e.g., by using abbreviations or other shorthand). *See id.* In addition, some funds may organize voting information based on the particular securities that each fund in the fund complex owns, while others may organize voting information based on the particular holdings of each fund. *See id.* As a result, a given fund's voting record can be spread throughout the report instead of presented together in one place. *See id.* N-PX reports are also not filed in a machine readable format, meaning investors must manually review them. *See id.* As a result, investors face significant challenges when trying to find a particular fund's voting record, find a specific vote or type of vote that is of interest, or compare funds' voting records. *See id.* Moreover, the current N-PX report does not provide investors with a complete picture of a fund's proxy voting practices, including with regard to its decision about whether to recall loaned shares in order to be able to vote them. *See id.* Information regarding the so-called lending-proxy voting tradeoff is likely to have substantial implications for shareholder democracy, corporate governance, and corporate stewardship. *See* Edwin Hu, Joshua Mitts & Haley Sylvester, *The Index Fund Dilemma: An Empirical Study of the Lending-Voting Tradeoff* 1 (N.Y.U. L. & Econ. Research Paper No. 20-52, 2020) ("We show that, after the SEC clarified funds' power to lend shares rather than vote them at shareholder meetings, institutions supplied 58% more shares for lending immediately prior to those meetings. The change is concentrated in stocks with high index fund ownership.").

[5] *See* Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, Release No. IC-25922 (Jan. 31, 2003) ("[W]e continue to believe that requiring funds to disclose their complete proxy voting records will benefit investors by improving transparency and enabling fund shareholders to monitor their funds' involvement in the governance activities of portfolio companies. . . . [R]egardless of whether all, or a majority of, investors are interested in proxy vote disclosure, we believe that fund shareholders who are interested in this information have a fundamental right to know how the fund has exercised its proxy votes on their behalf.").

[6] *See* Jonathon Zytnick, *"Do Mutual Funds Represent Individual Investors?"* (NYU L. & Econ. Research Paper No. 21-04 (March 7, 2021) ("finding evidence consistent with limited attention, in which the costs [to shareholders] of acquiring more granular detail about funds, as compared to readily available information, exceed the benefits.").

[7] *See id.* To the extent the proposed amendments lower the costs of acquiring more granular detail about funds, they have the potential to alter the existing cost-benefit analysis such that the costs may no longer exceed the benefits. This may increase the likelihood and incentive for investors to collect, analyze, and compare voting information.

[8] The proposal also has the potential to address the so-called "Problem of 12," the idea that "control of most public companies…will soon be concentrated in the hands of a dozen or fewer people." John C. Coates, *The Future of Corporate Governance Part I: The Problem of Twelve*, at 1 (Harvard Pub. L. Working Paper No. 19-07) (Sept. 20, 2018). Coates explains: "Twelve is an imprecise metaphor for a "small number"—for a given public company, the number might be even smaller, or modestly larger—but is the typical size of a public company board. In effect, indexation is concentrating power over all public companies in the hands of one board-sized group." *Id*. & n.1. He concludes that policymakers' goals should be "to preserve the agency-cost reducing impact that concentration of ownership in fewer hands has on portfolio companies, while addressing the potential agency costs, and legitimacy and accountability challenges that related concentration creates." *Id.* at 23. In short, the "Problem of 12" is the concern that the three largest index funds will increasingly own a significant percentage of

the stock market without any accountability, which is likely to increase agency costs. By promoting transparency of fund votes on corporate matters and enabling investors to monitor their funds' involvement in the governance activities of portfolio companies, the proposal has the potential to promote accountability and reduce agency costs, thereby potentially addressing concerns about the "Problem of 12."