

## [Securities Regulation Daily Wrap Up, TOP STORY—Commission adopts modified proxy adviser regulation and related robo-voting guidance, \(Jul. 22, 2020\)](#)

Securities Regulation Daily Wrap Up

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Regulations soon to be applicable to proxy advisers will require greater transparency about their conflicts of interest and greater access by registrants and clients to registrant comments on proxy voting advice.

The Commission adopted a somewhat less stringent regulation, as compared to an earlier proposal, to further regulate proxy advisory firms by mandating additional disclosures to ensure that proxy advice clients have access to material information about registrants. The regulation also allows registrants who are the subject of a proxy adviser's proxy voting advice to submit comments on that proxy voting advice. The Commission also issued guidance on the proxy voting responsibilities of investment advisers regarding pre-populated robo-voting services. The regulation and guidance were adopted by 3-1 votes, with Commissioner Allison Herren Lee dissenting in both instances (Exemptions from the Proxy Rules for Proxy Voting Advice, [Release No. 34-89372](#), July 22, 2020; Supplement to Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, [Release No. IA-5547](#), July 22, 2020).

**Commission more thoroughly regulates proxy advisers.** Proxy advisers are one of the last SEC constituencies not subject to more extensive regulation and have been the source of controversy for some time, especially regarding the influence of a select few such firms and allegations made by registrants about lack of transparency and conflicts of interest. Within the last few years, Congress had taken up the subject of proxy advisers on a bipartisan basis resulting in [varied legislative approaches](#) with the Republican-led House proposal being more draconian and the Senate's proposal taking a more modest approach. Into this milieu the SEC [proposed](#) a regulation more in line with the stringent House bill, but today adopted a somewhat less stringent regulation focused more on principles-based regulation of proxy advisers instead of the highly prescriptive proposal it had issued in November 2019.

A [press release](#) accompanying the new regulation said the enhanced regulation of proxy advisers codified the Commission's long-held view that proxy voting advice generally is a solicitation under federal securities regulations. SEC Chairman Jay Clayton [emphasized](#) that the proxy advisers regulation was the result of a "rigorous and well-functioning rulemaking process" and is designed to benefit MainStreet investors, especially given the significant influence of institutional investors who vote proxies. The reference to the rulemaking process may have been intended to address concerns voiced by Commissioner Lee that the Commission failed to adequately justify the need for the regulation.

Commissioner Elad Roisman, whom Clayton had [designated](#) to lead the agency's proxy reforms, emphasized, among other things, that registrants and proxy advisers' clients will have access to proxy advice at the same time and that clients will have access to registrants' responses to such proxy advice before they vote. "I believe the amendments we will vote on today will help provide consistent standards for conflict of interest disclosure as well as engagement with registrants. This consistency should improve the information available to investment advisers and other investors when they evaluate voting advice and make voting decisions," [said](#) Roisman.

According to Commissioner Hester Peirce, the new regulation is a "measured and appropriate change" to existing proxy rules. Peirce specifically [noted](#) that: "Indeed, careful consideration of the comments made it clear that the objectives of the proposal could be achieved by a less prescriptive and more principles-based approach."

Commissioner Lee, the lone dissenter, issued a [public statement](#) in which she reiterated concerns she had expressed when the Commission issued its proxy adviser proposal. Said Lee:

The final rules will still add significant complexity and cost into a system that just isn't broken, as we still have not produced any objective evidence of a problem with proxy advisory firms' voting recommendations. No lawsuits, no enforcement cases, no exam findings, and no objective evidence of material error—in nature or number. Nothing. \*\*\* While I appreciate the thought and effort by my colleagues that went into some of the changes, making the final rules less objectionable than the proposal does not relieve the Commission of its fundamental obligation to identify the need for this rulemaking and to explain how the rules we are adopting will meet this need.

**Proxy advice transparency.** The Commission majority approved amendments to Exchange Act Rule 14a-1(l) to define "solicitation" to include "the furnishing of a form of proxy or other communication to security holders under circumstances reasonably calculated to result in the procurement, withholding or revocation of a proxy, including: (A) Any proxy voting advice that makes a recommendation to a security holder as to its vote, consent, or authorization on a specific matter for which security holder approval is solicited, and that is furnished by a person that markets its expertise as a provider of such proxy voting advice, separately from other forms of investment advice, and sells such proxy voting advice for a fee." Rule 14a-1(l) also is amended to provide that "solicitation" does not include the "furnishing of any proxy voting advice by a person who furnishes such advice only in response to an unprompted request."

The Commission also added Exchange Act Rule 14a-2(b)(9), which provides that exemptions available in Rules 14a-2(b)(1) (solicitation on behalf of person who does not seek to act as proxy and does not act for a person seeking revocation or other objectives) and 14a-2(b)(3) (furnishing of proxy voting advice to a person with whom the advisor has a business relationship) are unavailable to a person who furnishes proxy voting advice unless two new requirements are met. The first of these requirements, contained in Rule 14a-2(b)(9)(i) requires a proxy voting advice business to disclose the following:

- Any information regarding an interest, transaction, or relationship of the proxy voting advice business (or its affiliates) that is material to assessing the objectivity of the proxy voting advice in light of the circumstances of the particular interest, transaction, or relationship; and
- Any policies and procedures used to identify, as well as the steps taken to address, any such material conflicts of interest arising from such interest, transaction, or relationship.

The second requirement, contained in Exchange Act Rule 14a-2(b)(9)(ii), requires a proxy voting advice business to adopt and publicly disclose written policies and procedures reasonably designed to ensure:

- Registrants that are the subject of the proxy voting advice have such advice made available to them at or prior to the time when such advice is disseminated to the proxy voting advice business's clients; and
- The proxy voting advice business provides its clients with a mechanism by which they can reasonably be expected to become aware of any written statements regarding its proxy voting advice by registrants who are the subject of such advice, in a timely manner before the security holder meeting (or, if no meeting, before the votes, consents, or authorizations may be used to effect the proposed action).

But a note to the requirement regarding policies and procedures states that the proxy voting advice business's written policies and procedures need not require it to make available to the registrant additional versions of its proxy voting advice with respect to the same meeting, vote, consent or authorization, as applicable, if the advice is subsequently revised. Moreover, a proxy voting advice business meets the requirement that it provide its proxy voting advice to a registrant if it provides the registrant with a copy of its proxy voting advice, at no charge, no later than the time such advice is disseminated to the proxy voting advice business's clients. However, the provision of proxy voting advice to a registrant may be conditioned on the following: (1) the registrant files its definitive proxy statement at least 40 calendar days before the security holder meeting date; and (2) the

registrant acknowledges that it will only use the proxy voting advice internally and/or in connection with the solicitation and will not publish or otherwise disseminate it beyond its employees or advisers.

A proxy voting advice business can satisfy the requirement that its clients have access to registrant statements about proxy voting advice by either: (1) notifying its clients via an electronic platform that the registrant intends to file (or has filed) additional soliciting materials with a hyperlink to those materials on EDGAR (when available); or (2) providing the same type of notice to clients via email or other electronic means with a hyperlink to those materials on EDGAR (when available).

However, Rule 14a-2(b)(9)(ii), regarding access by registrant and clients to proxy voting advice and registrant statement about that advice, does not apply to: (1) advice based on custom voting policies that are proprietary to a proxy voting advice business's client; or (2) recommendations in a solicitation subject to Rule 14a-3 regarding: (a) approval of a reclassifications, merger or consolidation, or transfers of assets under Securities Act Rule 145(a); or (b) solicitations by any person or group of persons for the purpose of opposing a solicitation subject to this regulation by any other person or group of persons.

**Proxy fraud amendment.** The new regulation amends Exchange Act Rule 14a-9 to include an additional note clarifying that the failure to disclose material information regarding proxy voting advice covered by Exchange Act Rule 14a-1(l)(1)(iii)(A), such as the proxy voting advice business's methodology, sources of information, or conflicts of interest, is an example of the types of activities that can be false or misleading within the meaning of Rule 14a-9. Rule 14a-9(a) provides for liability arising from the making of a solicitation by proxy statement that contains any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading.

**A note on compliance.** The SEC's new proxy adviser regulation is effective 60 days after publication in the *Federal Register*. However, compliance with some portions of the regulation will not be immediately required. Specifically, proxy voting advice businesses are not required to comply with amendments to Rule 14a-2(b)(9) until December 1, 2021. The Commission explained that this transition period is designed to allow proxy advisory businesses to establish newly required policies and procedures and to create other systems for compliance before the start of 2022 proxy season. The Commission also said the transition period is designed to avoid peak proxy season disruptions. The Commission further noted that early compliance would be welcomed.

However, the new regulation also contains definitional and antifraud provisions that are not included in the compliance transition period because they do not include new regulatory requirements that demand significant preparation for compliance. As a result, compliance with these provisions would be required when the regulation becomes effective.

Lastly, the new guidance on the proxy voting responsibilities of investment advisers is effective upon publication in the *Federal Register*.

**Robo-voting guidance.** The Commission also adopted related supplemental guidance addressing the issue of electronic or robo-voting. Specifically, the guidance addresses electronic vote management systems that can populate in advance an investment adviser's proxies with suggested voting recommendations and/or voting execution services and builds upon [prior guidance](#) about advisers' fiduciary duties issued in August 2019.

The guidance urges an investment adviser to consider disclosing: (1) the extent to which the adviser uses automated voting and the circumstances in which such voting methods are used; and (2) how the adviser's policies and procedures address automated voting in a situation where the adviser learns (before the submission deadline for voting proxies) that an issuer has or will file additional solicitation materials with the Commission. The guidance also urges an adviser to consider whether its policies and procedures are reasonably designed to address automated voting disclosures. Moreover, the guidance urges an adviser to consider its obligations

under Form ADV and Investment Advisers Act Rule 206(4)-6, which provides that it is a fraudulent, deceptive, or manipulative act, practice or course of business to fail to make certain disclosures regarding proxy voting.

**Industry reaction.** The Council of Institutional Investors issued a [press release](#) expressing relief that, in its view, the Commission dropped the most concerning aspects of the proposal but still retained provisions that could result in delays, increased costs, and threaten the independence of proxy advice. Specifically, the apparent need for investor clients to review issuer responses to proxy advice before voting would be problematic, the CII said. This was a point Commissioner Lee also had made in her dissenting statement.

Tom Quaadman, executive vice president at the Center for Capital Markets Competitiveness within the U.S. Chamber of Commerce, issued a [statement](#) in which he said the new proxy adviser regulation has the potential to counter a long decline in the number of U.S. public companies: "Today the SEC has acted to protect investors, promote transparency, end conflicts of interest and boost U.S. competitiveness through oversight of proxy advisory firms. These improvements will reorient shareholder proposals and director elections to ensure the long-term success of businesses and provide much needed returns for investors."

The releases are [Nos. 34-89372](#) and [IA-5547](#).

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