

**MEMO# 24259**

April 23, 2010

# Institute Testimony on Corporate Governance

[24259]

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TO: SEC RULES MEMBERS No. 36-10  
ETF ADVISORY COMMITTEE No. 15-10  
CLOSED-END INVESTMENT COMPANY MEMBERS No. 22-10  
SMALL FUNDS MEMBERS No. 26-10  
INVESTMENT COMPANY DIRECTORS No. 9-10    RE: INSTITUTE TESTIMONY ON CORPORATE GOVERNANCE

The House Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises recently held a hearing titled “Corporate Governance and Shareholder Empowerment.” [\[1\]](#) The Institute submitted testimony to the Subcommittee addressing four issues: proxy access; broker discretionary voting; disclosure of proxy votes; and mandatory independent board chairs. [\[2\]](#) The testimony is summarized below.

## **I. Shareholder Access to Company Proxy Materials**

### *A. Application of Proxy Access Requirements to Investment Companies*

The Institute’s testimony discussed how funds would be affected by a provision in a House bill that directs the Securities and Exchange Commission (“SEC”) to require, by rule, that issuers permit their shareholders to vote on candidates for the board of directors who have been nominated by shareholders who, in the aggregate, have owned at least one percent of the company’s voting securities for at least two years. [\[3\]](#)

The Institute stated that applying proxy access requirements indiscriminately to all issuers, including investment companies, fails to take into account the significant differences in governance models between public operating companies and investment companies. In addition, it fails to take into account that, unlike investors in operating companies, shareholders of investment companies are guaranteed the right to participate in key decisions.

The testimony opposed the proxy access provisions of H.R. 2861 and recommended that, should Congress pursue legislation confirming the SEC's authority to adopt proxy access requirements, such legislation also require the SEC to take into account relevant differences between operating companies and investment companies in applying any final proxy access rules to investment companies.

#### *B. Application of Proxy Access Requirements to Public Operating Companies*

The testimony opposed a federally mandate that would force all public companies, at their expense, to allow shareholders to nominate directors on a company's proxy statement, as would be provided by H.R. 2861. Rather, the SEC should be given the latitude to determine the exact contours of rules regarding whether, how, and in what circumstances shareholders will be permitted to nominate directors.

## **II. Elimination of Broker Voting on Uncontested Elections of Investment Company Directors**

The testimony discussed how a provision in H.R. 2861 directing the SEC to prohibit, by rule, the practice of brokers voting securities they hold on behalf of customers in uncontested director elections, in the absence of voting instructions from the customer, would affect investment companies. The testimony pointed out that this provision appears to be intended, in part, to codify a recent change to New York Stock Exchange Rule 452 that generally would prohibit broker discretionary voting for the uncontested election of directors. That rule change, however, expressly excepted registered investment companies, thereby permitting brokers to continue to vote such shares—a result that was reached through an extensive deliberative process.

The testimony stated that the drafters of H.R. 2861 may not have intended to override the NYSE's exception for registered investment companies, but that is exactly what it would do. This would be an extremely costly and unnecessary change for investment companies and their shareholders.

The testimony concluded that, while shareholder voting for directors is an important component of a strong corporate governance structure, prohibiting discretionary broker voting in the context of funds simply is not justified given the costs. For these reasons, the testimony strongly recommended that H.R. 2861 be revised to retain discretionary broker

voting with respect to funds.

### **III. Proxy Vote Disclosure**

The testimony strongly supported a provision in another House bill under consideration, H.R. 3351, [4] which would require every institutional investment manager to disclose, at least annually, all of its proxy votes. It pointed out that since 2004, funds—alone among all institutional investors—have been required to publicly disclose their proxy votes. H.R. 3351 would expand this transparency to all institutional investors, which the Institute has long advocated.

### **IV. Mandatory Independent Board Chair**

The testimony opposed provisions in H.R. 2861 and H.R. 3272 [5] that essentially would require every issuer to have an independent board chair. It pointed out that we are not aware of any substantial or reliable evidence of proven benefits that would justify imposing such a requirement on all public companies. Instead, we believe the selection of an appropriate person to serve as board chair rightfully is, and should continue to be, a decision made by the directors themselves.

Dorothy M. Donohue  
Senior Associate Counsel

#### **endnotes**

[1] Information about the hearing, including the testimony of the witnesses, is available on the House Financial Services Committee's website at [http://www.house.gov/apps/list/hearing/financialsvcs\\_dem/hrcm\\_041410.shtml](http://www.house.gov/apps/list/hearing/financialsvcs_dem/hrcm_041410.shtml). Testifying at the hearing were: [The Honorable Steven D. Irwin](#), Commissioner, Pennsylvania Securities Commissioner; [Gregory W. Smith](#), Chief Operating Officer and General Counsel, Colorado Public Employees' Retirement Association; [Mr. Thomas F. Brier](#), Deputy Chief Investment Officer and Director of Corporate Governance, Pennsylvania State Employees' Retirement System; [Mr. Alexander M. Cutler](#), Chairman and Chief Executive Officer, Eaton Corporation; [Mr. Brandon J. Rees](#), Deputy Director, Office of Investment, AFL-CIO; [Mr. Robert E. Smith](#), Vice President, Deputy General Counsel, and Assistant Secretary, NiSource on behalf of the Society of Corporate Secretaries and Governance Professionals; and [Mr. James Allen](#), Head of Capital Markets Policy, CFA Institute.

[2] See Statement of the Investment Company Institute on "Corporate Governance and Shareholder Empowerment" before the Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises, Committee on Financial Services, United States House of Representatives, dated April 21, 2010 available at [http://www.ici.org/policy/ici\\_testimony/10\\_house\\_corp\\_gov\\_tmny](http://www.ici.org/policy/ici_testimony/10_house_corp_gov_tmny).

[3] See Section 2 of H.R. 2861, the "Shareholder Empowerment Act of 2009."

[4] H.R. 3351 is titled the "Proxy Voting Transparency Act of 2009."

[5] H.R. 3272 is titled the “Corporate Governance Reform Act of 2009.”

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