

## COMMENT LETTER

March 15, 2019

# ICI Letter to the SEC on the Proxy Process (pdf)

March 15, 2019 Ms. Vanessa Countryman Acting Secretary Securities and Exchange Commission 100 F Street, NE Washington, DC 20549 Re: SEC Roundtable on the Proxy Process (File No. 4-725) Dear Ms. Countryman: The Investment Company Institute<sup>1</sup> supports the Commission's interest in examining proxy issues and applauds the Commission's decision to launch the effort with its recent roundtable on the proxy process ("Proxy Roundtable"). Proxy voting is important to registered investment companies (generally "regulated funds") in their dual roles as institutional investors and issuers. As institutional investors, regulated funds have specific proxy voting responsibilities with respect to their portfolio securities. In addition, regulated funds, unlike any other institutional investor, must publicly disclose their proxy votes. As issuers, regulated funds prepare proxy solicitation materials in connection with meetings of their shareholders and experience all of the challenges that accompany that process. Accordingly, ICI and its members have a strong interest in a well-functioning, cost-efficient proxy system. We believe the Commission's review of this complex system is particularly timely given the recent advances in communications technology. Based on the discussion and agenda at the Proxy Roundtable<sup>2</sup> and Chairman Clayton's December testimony to Congress,<sup>3</sup> it appears that the Commission is considering reforms related to:

- 1 The Investment Company Institute (ICI) is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI's members manage total assets of US\$21.9 trillion in the United States, serving more than 100 million US shareholders, and US\$6.6 trillion in assets in other jurisdictions. ICI carries out its international work through ICI Global, with offices in London, Hong Kong, and Washington, DC.
- 2 U.S. Securities and Exchange Commission Roundtable on the Proxy Process Transcript (Nov. 15, 2018), available at [www.sec.gov/files/proxy-round-table-transcript-111518.pdf](http://www.sec.gov/files/proxy-round-table-transcript-111518.pdf).
- 3 Testimony on Oversight of the US Securities and Exchange Commission, SEC Chairman Jay Clayton, before the US Senate Committee on Banking, Housing, and Urban Affairs (December 11, 2018), available at [www.sec.gov/news/testimony/testimony-oversight-us-securities-and-exchange-commission-0](http://www.sec.gov/news/testimony/testimony-oversight-us-securities-and-exchange-commission-0).

Ms. Vanessa Countryman March 15, 2019 Page 2 □ The role of proxy advisory firms; □ The shareholder proposal process; and □ Proxy voting mechanics and technology (or more colloquially, "proxy plumbing"). As the Commission and staff contemplate reform, we urge consideration of the Commission's specific regulatory framework applicable to regulated

funds under the Investment Company Act of 1940 and investment advisers under the Investment Advisers Act of 1940. These two statutes and the rules adopted thereunder have meaningfully shaped how regulated funds and their investment advisers vote proxies. We agree that there are opportunities to improve the proxy process. The Commission could explore ways to enhance transparency and accountability, such as through requiring institutional investors other than regulated funds to publicly disclose their proxy votes and facilitating better communication among issuers, proxy advisory firms, and investors. Other areas also are ripe for revision, such as the requirements for resubmitting shareholder proposals and determining whether a shareholder proposal may be excluded under Rule 14a-8. We strongly urge the Commission to consider how it can leverage technology to allow shareholders to confirm that their votes were tabulated consistent with their instructions. We hope our insights as both investors and issuers can be an asset as the Commission more fully considers regulatory refinements to address some of the issues raised at the Proxy Roundtable.

I. Regulated Funds and Advisers: Proxy Voting

Requirements and Practice Over 15 years ago, the Commission adopted rules that have been critical in shaping how regulated funds vote their portfolio company proxies.<sup>4</sup> Since 2004, regulated funds (but not any other institutional investor) have publicly reported their proxy votes to the SEC, providing a full and transparent record of how they have voted proxies.<sup>5</sup> Regulated funds also must describe in their registration statements the policies and procedures that they use to determine how to vote proxies for their portfolio securities.<sup>6</sup> The Commission further requires a fund adviser with proxy voting authority to adopt and implement proxy voting policies and procedures reasonably designed to ensure that it votes client proxies in the best interest of its clients. The adviser must describe its policies and procedures in Part 2 of its Form ADV. 4 Proxy Voting by Investment Advisers, SEC Release No. IA-2106 ( Jan. 31, 2003), available at [www.sec.gov/rules/final/ia-2106.htm](http://www.sec.gov/rules/final/ia-2106.htm); and Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, SEC Release No. IC-25922 ( January 31, 2003), available at [www.sec.gov/rules/final/33-8188.htm](http://www.sec.gov/rules/final/33-8188.htm). 5 Investment Company Act Rule 30b1-4 and Form N-PX. The requirements were effective as of April 14, 2003, and funds were required to file their first report on Form N-PX not later than August 31, 2004, for the twelve-month period beginning July 1, 2003 and ending June 30, 2004. 6 Item 17(f ) of Form N-1A (registration statement for open-end funds), Item 18 of Form N-2 (registration statement for closed-end funds), and Item 20 of Form N-3 (registration statement for separate accounts organized as management investment companies). Closed-end funds also must include similar disclosure under Item 7 of their annual Form N-CSR filings. Ms. Vanessa Countryman March 15, 2019 Page 3 Further, the policies and procedures must address how the adviser will handle material conflicts of interest between it and its clients.<sup>7</sup> The SEC's engagement on these issues has continued since its 2003 rulemakings, as evidenced by the staff resources it has devoted to providing guidance and overseeing proxy voting. In 2014, the staff issued proxy-related guidance to investment advisers and proxy advisory firms.<sup>8</sup> And the staff has examined investment advisers' compliance with their fiduciary duty in voting proxies, as well as certain proxy advisory firms and how they make recommendations and disclose and mitigate conflicts.<sup>9</sup> Regulated funds are notable in the role that their boards of directors play in proxy voting. A fund's board is responsible for voting the proxies relating to the fund's portfolio securities. The board typically delegates this day-to-day responsibly to the fund's adviser, which the adviser carries out in accordance with the fund's board-approved proxy voting policies and procedures.<sup>10</sup> This delegation is subject to the board's continuing oversight of the fund adviser, and proxy voting policies and procedures are part of the compliance programs that the board reviews under Investment Company Act Rule 38a-1. Regulated funds must, and do, take their proxy voting responsibilities seriously. The fund industry devotes substantial resources to this

function. During the 2017 proxy voting season, funds cast more than 7.6 million votes for proxy proposals, and the average mutual fund voted on 1,504 separate proxy proposals.<sup>11</sup> These numbers represent only funds' proxy voting activity for their US-listed portfolio companies.<sup>12</sup> Many funds also invest in portfolio companies domiciled outside the US—for them, proxy voting responsibilities are even more expansive and complex. In 2017, one member cast nearly 7 Advisers Act Rule 206(4)-6 applies to all registered investment advisers. An adviser also must (i) disclose how clients may obtain information about how the adviser voted with respect to their securities, and (ii) provide clients with a copy of its proxy voting policies and procedures to clients upon request. <sup>8</sup> See *infra*, note 21, and accompanying text. <sup>9</sup> See, e.g., SEC Office of Compliance Inspections and Examinations ("OCIE"), Examination Priorities for 2015, available at [www.sec.gov/about/offices/ocie/national-examination-program-priorities-2015.pdf](http://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2015.pdf) (proxy services as an examination priority); OCIE, Compliance Alert, July 2008, available at [www.sec.gov/about/offices/ocie/complialert0708.htm](http://www.sec.gov/about/offices/ocie/complialert0708.htm) (describing reviews of practices with respect to use of third party proxy voting services); and OCIE, Highlights, February 3, 2010, available at [www.sec.gov/about/offices/ocie/ocie\\_highlights.shtml](http://www.sec.gov/about/offices/ocie/ocie_highlights.shtml) (during routine inspections staff has focused on proxy voting policies, including to ensure disclosures were consistent with votes cast). <sup>10</sup> A fund board may adopt separate fund policies and procedures or may adopt or rely on the adviser's policies and procedures. <sup>11</sup> Funds and Proxy Voting: Funds Vote Thoughtfully and Independently, ICI Viewpoints (Nov. 7, 2018), available at [www.ici.org/viewpoints/view\\_18\\_proxy\\_voting\\_results](http://www.ici.org/viewpoints/view_18_proxy_voting_results). This 7.6 million figure is the total number of proxy votes cast by funds during proxy season 2017. If, for example, there were two affiliated funds casting proxy votes for a company that had 10 proposals on its ballot, the total number of votes would be 20 (equal to two funds casting proxy votes times 10 proxy proposals). <sup>12</sup> ICI's data set included fund proxy voting information only for those companies included in the Russell 3000 Index. The Russell 3000 Index tracks the performance of the 3,000 largest stocks traded in the US and represents approximately 98 percent of US stock market capitalization. Ms. Vanessa Countryman March 15, 2019 Page 4 160,000 proxy votes in connection with over 17,000 shareholder meetings across 82 countries. Due to the large number of portfolio securities that funds may hold in the US and abroad, efficient and informed proxy voting is a large undertaking and substantial responsibility. As fund advisers' investment management styles differ, so too do their approaches for gathering and processing relevant information related to their large and diverse proxy voting responsibilities. Fund advisers do not use a single technique for deciding how to vote proxies. Some fund advisers utilize individuals, teams, or committees<sup>13</sup> specifically dedicated to analyzing proposals and voting proxies. Others may look to the individual fund portfolio managers to make voting decisions. The analytical approach that fund advisers typically take to proxy votes may differ depending on the proposal's subject matter and nature. For recurring matters, a fund's proxy voting guidelines typically will indicate, or provide a starting point for, how the fund will cast votes on various types of proxy proposals. For instance, the guidelines may specify the circumstances under which the fund generally will vote for or against uncontested director nominees or independent auditors. These fund guidelines reflect the independent views of the fund adviser and board about how to act in the best interest of the fund.<sup>14</sup> Consistent with staff guidance, fund advisers and fund boards review their guidelines, including any material changes, at least annually.<sup>15</sup> In addition to providing transparency to investors and others, proxy voting guidelines allow funds to handle with efficiency the large majority of votes that are recurring and non-controversial, and thereby prioritize and spend more time on the smaller percentage of those that are not. As depicted in Figure 1 below, ICI's analysis of the 2017 proxy season indicates that the vast majority of proxy proposals were management proposals (over 98 percent), and most of those management proposals (80

percent) were votes on uncontested elections of directors or ratification of a company's audit firm. 13 A fund adviser with a more centralized approach to proxy voting still may grant others (e.g., portfolio managers or analysts) input or even ultimate discretion in how the adviser votes fund proxies. 14 Many funds include their guidelines in their registration statements, or otherwise make them available on firm websites. A fund adviser may use guidelines for multiple clients, including the funds it manages. See *supra*, note 10. 15 See the bulletin, *infra* note 21, which states the staff's view that "as part of an investment adviser's ongoing compliance program, it should review, no less frequently than annually, the adequacy of its proxy voting policies and procedures to make sure they have been implemented effectively, including whether these policies and procedures continue to be reasonably designed to ensure that proxies are voted in the best interests of its clients." (citing Advisers Act Rule 206(4)-7 and Investment Company Act Rule 38a-1). Ms. Vanessa Countryman March 15, 2019 Page 5

Figure 1: Proxy Proposals for the Largest Publicly Traded US Companies, 2017 Percent of total

Note: This figure represents proxy proposals for companies in the Russell 3000 Index with shareholder meetings from July 1, 2016, to June 30, 2017. Source: Investment Company Institute tabulations of ISS Corporate Services data

This assessment is similar to ICI's analysis of the 2007-2009 US proxy seasons: in 2009, the vast majority of proxy votes (over 85 percent) were on director elections and auditor ratifications.<sup>16</sup> Given this, proxy voting guidelines provide valuable criteria for funds to use in determining how to cast the overwhelming majority of their votes. Guidelines also provide direction for identifying matters that warrant even greater analysis (e.g., "case-by-case" analysis of proposed mergers, contested director elections, and certain shareholder proposals). As part of an in-depth review, the fund adviser can use information in the proxy statement, any supplemental proxy materials, and information from other sources.<sup>17</sup> Above all, the fund adviser's goal is to cast the fund's votes in a manner that best advances the interests of the fund and its shareholders. Numerous factors and considerations help the fund adviser arrive at its voting decisions, and may include the following for management or shareholder proposals, depending on the type:

- What are the details of the proposal?

16 See ICI Perspective: Trends in Proxy Voting by Registered Investment Companies 2007-2009, available at [www.ici.org/pdf/per16-01.pdf](http://www.ici.org/pdf/per16-01.pdf). 17 The proxy statement and supplemental proxy materials include descriptions of the voting matters, company analysis, and management's voting recommendations (including on shareholder proposals that management opposes). Ms. Vanessa Countryman March 15, 2019 Page 6

- How does this proposal align with the strategy of the company?
- What is management's view of the proposal? What are the views of other relevant parties?
- Is the proposal one that the company can implement effectively?
- What would the economic consequences of the proposal be to the company? If adopted, would the proposal impose material costs on the company? What would the anticipated benefits be relative to those anticipated costs?
- Would any unanticipated consequences result from the proposal's adoption?

Shareholder proposals may include the following additional considerations:

- Does the proposal address the general interests of the company's shareholders, or just those of the shareholder proponent(s)?
- Has the company engaged with the shareholder proponent(s)?
- Has the company provided sufficient information and/or adequately addressed the proposal, either in existing disclosure or in its proxy statement?
- Is the proposal specific to certain facts and circumstances of the company, or is the subject matter generic and applicable to all publicly-traded companies or companies in a specific industry?
- Has this proposal appeared on the company's proxy statement in previous years and failed to garner significant shareholder support?
- How is the company currently handling the issue motivating the proposal (including relative to its peers), and would the issue better be addressed through legislation or regulation?

While the percentage of annual votes on recurring matters is significantly larger than the percentage of other votes, in absolute

terms funds still vote on a large and diverse number of non-routine matters,<sup>18</sup> as Figure 2 below illustrates: 18 In this letter, we use the term “non-routine” to refer all types of proxy matters except for director elections and auditor ratifications (simply because both occur annually; the term is not intended to convey the relative importance of any vote). In contrast, NYSE Rule 452 would categorize director elections as “non-routine.” Ms. Vanessa Countryman March 15, 2019 Page 7 Figure 2: Non-Routine Proxy Proposals for the Largest Publicly Traded US Companies, 2017 \*Includes director-related proposals. Note: This figure represents proxy proposals for companies in the Russell 3000 Index with shareholder meetings from July 1, 2016, to June 30, 2017. Source: Investment Company Institute tabulations of Form N-PX data and ISS Corporate Services data Even non-routine matters that superficially appear similar to one another may be quite nuanced and lead funds to vote, in the aggregate, for or against proposals in very different ways, based on their assessments of all relevant facts and circumstances. For instance, Figure 3 below shows the percentage of funds that voted “for” certain proposals that incorporated specific language about the goal of limiting global warming to the 2 degrees Celsius threshold established by the 2015 Paris Climate Accord. These proposals were submitted to 23 companies across a range of industries in proxy season 2017 and called for companies to generate reports to shareholders either about the impacts of climate change on the company’s business, or the company’s efforts to address global warming. The bars indicate the varying levels of fund support that each received, and whether each passed or failed (green bars denote proposals that passed). And just as outcomes across company proposals differ, funds themselves differ in their conclusions on specific proposals. Ms. Vanessa Countryman March 15, 2019 Page 8 Figure 3: Fund Votes and Outcomes on Certain Climate-Related Proposals Percentage of funds voting “For” the proposal Source: Investment Company Institute tabulations of ISS Corporate Services data II. Regulated Funds and Advisers: Use of Proxy Advisory Firms A. Proxy Advisory Firm Services Many (but not all) fund complexes hire proxy advisory firms as vendors to assist them in carrying out their proxy voting responsibilities. Reflecting the varying scale of proxy voting responsibilities and the different needs of investors, proxy advisory firms offer a range of services including: □ Assisting with the administrative tasks associated with proxy voting, including keeping track of meeting dates, reconciling clients’ holdings, reconciling ballots, and setting up and closing the various accounts that a single client may maintain on behalf of its clients; □ generating proxy voting reports; □ reorganizing proxy statements in a standardized format so that investors can efficiently analyze the statements’ contents; □ preparing research reports and providing their general recommendations on whether to vote “for,” “against,” or “abstain” on specific proxy proposals;<sup>19</sup> □ generating custom recommendations for clients, based on clients’ own proxy voting guidelines; □ submitting votes through platforms in accordance with clients’ instructions; and <sup>19</sup> Some fund complexes may consult multiple proxy advisory firms’ reports. Ms. Vanessa Countryman March 15, 2019 Page 9 □ compiling information for funds’ annual proxy voting filings with the SEC on Form N-PX. Funds and their advisers may avail themselves of one or more of these services, e.g., by using these vendors for administrative services and research, but not consulting their general vote recommendations. Those fund advisers that consult proxy advisory firms’ research and recommendations may consider this information to varying degrees, along with views of management and other investors and shareholder proponents. Fund advisers also may directly engage with portfolio companies on a variety of matters and take this engagement into account in deciding how to vote.<sup>20</sup> Given the complexity and range of fund proxy voting responsibilities, many fund advisers understandably value the administrative and research services that proxy advisory firms offer. B. SEC Staff Guidance on Proxy Advisory Firms Acknowledging the role of proxy advisory firms, the staff of the Divisions of Corporation Finance and Investment Management issued a bulletin in 2014 that provides

guidance about investment advisers' proxy voting responsibilities generally and the exemptions to the federal proxy rules that proxy advisory firms commonly rely upon.<sup>21</sup> The bulletin expresses the staff's view that in retaining a proxy advisory firm, an investment adviser should assess whether the firm has the "capacity and competency to adequately analyze proxy issues." Moreover, an investment adviser should "provide sufficient ongoing oversight" of these firms to ensure that the investment adviser continues to vote proxies in the best interests of its clients.<sup>22</sup> In September, the staff invited information and feedback from stakeholders on the bulletin.<sup>23</sup> The bulletin is a useful resource for fund complexes and others, and we strongly recommend that the SEC retain it. Following issuance of the bulletin, ICI conducted an industrywide assessment of funds' 20 See e.g., BlackRock May 31, 2017 press release, available at [www.blackrock.com/corporate/literature/press-release/blk-vote-bulletin-exxon-may-2017.pdf](http://www.blackrock.com/corporate/literature/press-release/blk-vote-bulletin-exxon-may-2017.pdf) (describing engagement with portfolio company which informed proxy voting decision); and Allianz Global Investors' materials and information about investment stewardship, available at <https://us.allianzgi.com/en-us/our-firm/esg/active-stewardship>. 21 Proxy Voting: Proxy Voting Responsibilities of Investment Advisers and Availability of Exemptions from the Proxy Rules for Proxy Advisory Firms, Staff Legal Bulletin No. 20 ( June 30, 2014) (the "bulletin"), available at [www.sec.gov/interp/leg/cfslb20.htm](http://www.sec.gov/interp/leg/cfslb20.htm). 22 This guidance is consistent with existing fund practices. As entities with typically no employees of their own, funds rely on the services of outside entities to function day-to-day. Continued oversight of key service providers—by both fund boards and advisers—is critically important, and is deeply ingrained in practice and regulation. See generally Board Oversight of Certain Service Providers, Independent Directors Council Task Force Report ( June 2007), available at [www.idc.org/pdf/21229.pdf](http://www.idc.org/pdf/21229.pdf); and Oversight of Fund Proxy Voting, Independent Directors Council and Investment Company Institute ( July 2008), available at [www.ici.org/pdf/ppr\\_08\\_proxy\\_voting.pdf](http://www.ici.org/pdf/ppr_08_proxy_voting.pdf). See also Investment Company Act Rule 38a-1(a)(3) (requiring annual review of "the adequacy of the policies and procedures of the fund and of each investment adviser, principal underwriter, administrator, and transfer agent and the effectiveness of their implementation"). 23 See Division of Investment Management Statement Regarding Staff Proxy Advisory Letters (September 13, 2018), available at [www.sec.gov/news/public-statement/statement-regarding-staff-proxy-advisory-letters](http://www.sec.gov/news/public-statement/statement-regarding-staff-proxy-advisory-letters). Ms. Vanessa Countryman March 15, 2019 Page 10 use of proxy advisory firms and published findings to outline concretely how fund advisers can and do fulfill the bulletin's guidance.<sup>24</sup> Investment advisers have developed sound due diligence and oversight practices consistent with this guidance—withdrawal of it, without anything in its place, would create uncertainty among investment advisers.<sup>25</sup> III. Proxy Voting: Transparency and Accountability A. New Regulatory Disclosure Requirements: Enhancing Transparency and Accountability Unlike any other shareholder, regulated funds publicly report all their proxy votes cast. In addition to providing narrative disclosure about how they vote proxies in their registration statements, regulated funds file annual Form N-PX filings, which report how funds actually voted on each matter during the prior year. Together, the requirements provide a complete picture of regulated funds' proxy voting practices and altogether outstrip any disclosure required of, or provided by, any other institutional investors. To the extent that disclosing proxy voting records achieves important public policy purposes, then all institutional investors should do so.<sup>26</sup> We therefore recommend that the SEC consider requiring certain other institutional investors to disclose how they use the corporate franchise.<sup>27</sup> Other institutional investors constitute a large part of the ownership of our public capital markets. As indicated in Figure 4 below, as of December 31, 2017 US-regulated funds' overall share of US corporate equity was less than a third (31 percent), pointing to the importance of other institutional shareholders in the proxy voting landscape.

24 Report on Funds' Use of Proxy Advisory Firms, Investment Company Institute and Independent Directors Council ( January 2015), available at [www.ici.org/pdf/pub\\_15\\_proxy\\_advisory\\_firms.pdf](http://www.ici.org/pdf/pub_15_proxy_advisory_firms.pdf). 25 If the SEC wishes to modify the bulletin's guidance in any way, we request that it publish such revisions for comment. 26 It has been the Institute's longstanding position that institutional investors other than regulated funds should disclose their proxy votes. See, e.g., Testimony of Paul Schott Stevens, President and CEO, Investment Company Institute, On SEC Proxy Access Proposals: Implications for Investors before the Committee on Financial Services, US House of Representatives (Sept. 27, 2007), available at [www.ici.org/proxy\\_voting/statements/testimonies/07\\_house\\_proxy\\_tmny#m](http://www.ici.org/proxy_voting/statements/testimonies/07_house_proxy_tmny#m). 27 We strongly recommend that, in doing so, the Commission consider how to minimize burdens on reporting entities and protect the privacy of investment advisers' clients. For instance, the Commission could explore amending Form 13F to require institutional investment managers that exercise investment discretion over \$100 million or more in "Section 13(f ) securities" to disclose, in the aggregate, how the manager voted on each proxy matter. Cf. HR 3351, Proxy Voting Transparency Act of 2009 (which would require, among other things, that every institutional investment manager subject to section 13(f ) report at least annually how it voted), available at [www.congress.gov/bill/111th-congress/house-bill/3351/text](http://www.congress.gov/bill/111th-congress/house-bill/3351/text). Ms. Vanessa Countryman March 15, 2019 Page 11 Figure 4: Domestic Equity by Holders Percent, year-end 2017 <sup>1</sup>Includes foundations, endowments, and hedge funds. <sup>2</sup>Represents direct holdings of US corporate equity in state & local and private pension plans and the Thrift Savings Plan; excludes RICs. Sources: Investment Company Institute, Federal Reserve Board, and World Federation of Exchanges Ironically, calls to increase proxy voting transparency tend to be paired with policy ideas focusing on regulated funds, even though they are the most transparent sub-set of institutional shareholders.<sup>28</sup> If the SEC's objective is greater transparency, then the SEC should focus on requiring a larger swath of institutional shareholders to disclose proxy voting data, rather than requiring regulated funds to provide more detailed information.<sup>29</sup> B. "Pass Through" Proxy Voting Is Utterly Impractical and Misguided One notion that has been part of the current dialogue is that retail fund investors should "have a say" in how funds vote proxies for their portfolio securities.<sup>30</sup> While no proponent has outlined this concept in 28 See, e.g., Common Ownership: The Investor Protection Challenge of the 21st Century, Testimony Before the Federal Trade Commission Hearing on Competition and Consumer Protection, Commissioner Robert J. Jackson Jr., Dec. 6, 2018, available at [www.sec.gov/news/testimony/jackson-testimony-ftc-120618](http://www.sec.gov/news/testimony/jackson-testimony-ftc-120618). In this speech, Commissioner Jackson first calls for "shining light on how institutions vote Americans' money" and then suggests that funds should provide additional disclosure regarding proxy voting (e.g., "requiring clearer, summary disclosure of the voting behavior of institutional investors relative to other voters' views"). 29 In our view, the amount, kind, and prominence of proxy-related disclosures that the Commission already requires regulated funds to provide is appropriate for them (as it would be for other institutional investors). Saddling regulated funds uniquely with additional disclosure obligations would only compound the existing inappropriate disparities among the obligations of institutional investors and perpetuate the current opacity about, in Commissioner Jackson's words, "how institutions vote Americans' money." 30 See, e.g., Main Street Investors Coalition, Empty Voting by Mutual Funds Threatens Shareholder Value ( July 2018), available at <https://mainstreetinvestors.org/empty-voting-by-mutual-fund-advisors-threatens-shareholder-value/>. Chairman Clayton may have been alluding to this idea in his statement announcing the Proxy Roundtable. See Statement Announcing SEC Staff Ms. Vanessa Countryman March 15, 2019 Page 12 any detail, the idea is that a regulated fund would be allowed to vote its portfolio company proxies only after the fund asks its own shareholders

how the fund should vote, essentially “passing through” the myriad of fund voting decisions in some fashion to fund shareholders. The SEC certainly should not require regulated funds to “pass through” proxy votes related to their portfolio securities to fund shareholders. The idea is altogether misguided and impractical, in view of the hundreds or thousands of proxy votes that a single fund may cast in a year; the thousands, or even millions, of shareholders that a fund might be required to contact to solicit voting feedback; and the existing communications and plumbing-related limitations that presently characterize the proxy system.<sup>31</sup> In his Proxy Roundtable announcement, Chairman Clayton noted the “relatively low retail participation rate” in voting proxies. This is a legitimate observation. As issuers, funds encounter substantial difficulties when they seek shareholder participation in funds’ proxy votes. It can take several months for a fund just to achieve quorum for a shareholder meeting, often at great expense and effort (e.g., phone call campaigns to solicit the necessary votes from shareholders who do not return their proxies) to the fund. It would defy all logic and empirical evidence, then, to suggest that there is pent-up demand among these same fund investors to weigh in personally on the hundreds or thousands of proxy votes that a fund casts each year. And because investors often hold shares in more than one fund, the burdens on fund shareholders would be multiplied by the number of equity-holding funds in which they invest. Investors value funds in large part because of their convenience, cost-efficiency, and seamless packaging of investment management services (including proxy voting). Unbundling these services and asking all shareholders to assume this new responsibility—and pay the enormous initial and ongoing expenses— would severely and adversely affect funds’ inherent appeal to retail investors.

IV. Proxy Roundtable Discussion: Proxy Advisory Firms

The Proxy Roundtable included a panel focused on proxy advisory firms. The panel considered several issues, including how investment advisers use proxy advisory firms, the ability of issuers to raise concerns with proxy advisory firms’ recommendations, and the appropriate regulatory regime for proxy advisory firms. Chairman Clayton’s Congressional testimony indicated that the SEC is exploring whether investors have effective access to company views on proxy advisory firms’ reports and recommendations. Roundtable on the Proxy Process ( July 30, 2018), available at [www.sec.gov/news/public-statement/statement-announcing- sec-staff-roundtable-proxy-process](http://www.sec.gov/news/public-statement/statement-announcing- sec-staff-roundtable-proxy-process), which expressed interest in “better understand[ing] ... [h]ow existing rules or market practices affect the ability of individuals who invest in the public markets through investment vehicles such as mutual funds and pension funds to participate in the governance of public companies in which they have an interest.” We were pleased that the idea was not discussed at the Proxy Roundtable, which we attribute to growing awareness of its serious defects. <sup>31</sup> For a more detailed critique of this idea, see SEC Should Reject Complex, Costly “Pass-Through” Proxy Voting, ICI Viewpoints (Oct. 2, 2018), available at [www.ici.org/viewpoints/view\\_18\\_passthrough\\_voting](http://www.ici.org/viewpoints/view_18_passthrough_voting). Ms. Vanessa Countryman March 15, 2019 Page 13 A.

Improving Communications Among Public Companies, Proxy Advisory Firms, and Investors

As described above, fund advisers rely on the information that companies provide to them directly (e.g., through proxy materials and other means) and also may consider research and recommendations from proxy advisory firms. Companies and proxy advisory firms also communicate with one another, in varying ways. Constructive communication among all these parties is important to fund advisers. If the Commission is intent on considering ways of improving the status quo, then it must be mindful of the prerogatives of fund advisers. Fund advisers expect and must receive independent, objective, and accurate information from proxy advisory firms. Timeliness also is a crucial consideration. In the current compressed proxy voting schedule, any response that a company wishes to make to a proxy advisory firm’s recommendation—to the proxy advisory firm and/or its shareholders—must occur promptly, so that investors can consider it prior to casting their votes. Finally, any required changes to current



communications flows or systems that are overly complex or otherwise difficult to administer could significantly increase costs. If proxy advisory firms are given additional responsibilities (e.g., to push out company views), their paying customers—fund advisers and other institutional investors—likely will shoulder such costs. Subject to these crucial qualifications, we are open to exploring mechanisms by which companies’ objections to proxy advisory firms’ research and recommendations could be put in front of investors in a more timely and convenient way. For instance, the Commission could explore ways that proxy advisory firms could “push” company views to their clients rather than relying on their clients to “pull” the information, as is often the case today.<sup>32</sup> If done carefully, such a process could benefit: □ investors—they would have a more complete, and easily accessible, “record” prior to casting votes, which would be particularly helpful in compressed proxy seasons; □ companies—it would open another channel of communication to shareholders and allow for better visibility of their comments on, or views of, proxy advisory firm recommendations; and □ proxy advisory firms—it would help dispel notions, real or perceived, about the accuracy of the recommendations and their willingness to engage.

<sup>32</sup> Companies already have channels to communicate their views on proxy matters to shareholders, most notably the proxy statements themselves. And they can voice their objections to proxy advisory firm reports through supplemental proxy filings, or direct communication with shareholders or proxy advisory firms. But we question whether this is an optimal arrangement for all involved. For example, it requires considerable work on the part of investors who, if they are not contacted directly, must comb company websites and/or EDGAR to determine if companies have raised any material objections to proxy advisory firm reports, all within highly compressed voting periods. Ms. Vanessa Countryman March 15, 2019 Page 14 The details accompanying any such proposed mechanism matter greatly. Consequently, the Commission must carefully consider options for making this information more easily available and readily visible to investors in the least burdensome way possible for all involved.

<sup>33</sup> B. Promote Enhanced Competition in a Balanced Manner The SEC also must consider the potential impact that any regulation may have on competition, including the ability for new firms to enter the proxy advisory industry. New firms would bring increased choice, diversity in analytical and philosophical perspectives, and the possibility of lower costs and greater innovation. Experience demonstrates, however, that overly-burdensome regulation impedes, rather than promotes, competition. In enacting the Credit Rating Agency Reform Act of 2006, Congress sought to “improve ratings quality for the protection of investors and in the public interest by fostering accountability, transparency, and competition in the credit rating agency industry.”<sup>34</sup> (Emphasis added.) Unfortunately, the new regulatory regime for credit ratings agencies did not increase competition, and in fact only one new entity has registered in the past dozen or so years. Today, three firms continue to dominate the credit ratings market.<sup>35</sup> We urge the SEC to consider carefully the costs and benefits of regulation as it contemplates the regulation of proxy advisory firms.

V. Proxy Roundtable Discussion: Rule 14a-8 and Shareholder Proposals Rule 14a-8 under the Exchange Act conditionally permits a company’s shareholders to include proposals (i.e., recommendations or requirements that a company and/or its board take action) on a company’s proxy statement. The Proxy Roundtable included a panel dedicated to exploring shareholder proposals and effective shareholder engagement. Chairman Clayton said that the SEC should consider reviewing the resubmission thresholds and related criteria for shareholder proposals. We agree that it is timely to review the thresholds and related criteria.

<sup>33</sup> We recognize that technological improvements to the overall proxy voting system could facilitate development of enhanced communication channels in a cost-efficient manner. We therefore support the SEC taking steps to encourage such advances.

<sup>34</sup> Public Law 109-291: Credit Rating Agency Reform Act of 2006.

<sup>35</sup> See Annual Report on Nationally Recognized Statistical Rating

Organizations, Staff of the U.S. Securities and Exchange Commission (December 2018), available at [www.sec.gov/files/2018-annual-report-on-nrsros.pdf](http://www.sec.gov/files/2018-annual-report-on-nrsros.pdf) (reporting that in 2017, the combined revenues of S&P, Moody's, and Fitch accounted for 94.1 percent of all nationally recognized statistical rating organizations' revenues for that fiscal year). Ms. Vanessa Countryman March 15, 2019 Page 15 A. Improve Resubmission Criteria Rule 14a-8(i) provides 13 bases upon which a company may exclude a shareholder proposal, including a "resubmissions" exclusion.<sup>36</sup> We would support the Commission increasing the minimum shareholder approval percentages and urge the Commission to use data derived from its experience in administering the resubmission exclusion to formulate reasonable amounts.<sup>37</sup> Alternatively, or in addition, the Commission also should explore the feasibility of a meaningful "time out" from including a shareholder proposal on a proxy if the proposal has not demonstrated sufficient momentum in gaining shareholder support over successive years.<sup>38</sup> The SEC's 1997 policy rationale—that the resubmission thresholds should permit exclusion of proposals that stand "no significant chance" of obtaining shareholder approval—remains valid.<sup>39</sup> The SEC should consider increasing these thresholds or other options that would advance the purposes of the rule's resubmission exclusion. Placing limits on resubmissions is a classic regulatory line-drawing exercise. Any limits should recognize that each time a shareholder proposal is resubmitted, companies and shareholders alike bear real costs. While shareholder proposals represent a small percentage of overall proxy matters, they often take a disproportionate amount of time compared to annual management

<sup>36</sup> This provides that for a shareholder to be eligible to resubmit the same (or a similar) proposal, the proposal must have received at least 3, 6, and 10 percent shareholder approval for the first, second, and third submissions, respectively, each within the preceding 5 calendar years. <sup>37</sup> While we do not advance a view on specific threshold levels, we note that in 1997, the SEC proposed raising the current 3 percent, 6 percent, and 10 percent shareholder support thresholds to 6 percent, 15 percent, and 30 percent, respectively, but it never adopted those changes. Amendments to Rules on Shareholder Proposals, SEC Release No. 34-39093 (Sept. 18, 1997), available at [www.sec.gov/rules/proposed/34-39093.htm](http://www.sec.gov/rules/proposed/34-39093.htm). In this proposing release, the SEC stated, "We propose to raise the thresholds to 6% on the first submission, 15% on the second submission, and 30% on the third. At least for the time frame contemplated by the rule, we believe that a proposal that has not achieved these levels of support has been fairly tested and stands no significant chance of obtaining the level of voting support required for approval. We propose to increase the second and third thresholds by relatively larger amounts because the proposal will have had two or three years to generate support." <sup>38</sup> If the SEC were to explore this "time out" option, it must specify its triggering conditions and length. This option also should be accompanied by further rule amendments to permit the exclusion of a proposal that is substantially similar to one that has recently been considered. In other words, the exclusion should be based on the substance of the proposal rather than the identity of the shareholder proponent (i.e., if Shareholder A were unsuccessful with a proposal and subject to a "time out," a company could exclude both Shareholder A's proposal and Shareholder B's substantially similar proposal during that time out). This would be similar to the "duplication" exclusion, which a company may rely on "[i]f the proposal substantially duplicates another proposal previously submitted to the company by another proponent that will be included in the company's proxy materials for the same meeting." Finally, once a proposal completes its time out, it should be subject to the highest shareholder approval percentage requirement going forward, i.e., it should not restart at the lowest percentage (currently, 3 percent). <sup>39</sup> See *supra*, note 37. Ms. Vanessa Countryman March 15, 2019 Page 16 proposals. "Zombie" proposals that appear on proxy statements year after year may distract investors from the analysis of other proxy votes. At the same time, we agree that shareholder proposals are a key means of engaging with

management; that in some cases, they have improved (and offer the possibility of further improving) governance; and, importantly, that some proposals take time to gain traction. At a certain point, however, a failed proposal's costs outweigh its potential benefits, particularly for serially-unsuccessful proposals where any benefits are unlikely to be realized but the associated costs are certain. Accordingly, we urge the Commission to seek to strike the right balance between these competing interests.

**B. Revamp the Exclusion Request Process** In addition to "resubmissions," Rule 14a-8(i) provides 12 other bases upon which a company may exclude a shareholder proposal. Some of the more noteworthy and contentious include the "relevance," "management functions," "conflicts with company's proposal," and "substantially implemented" exclusions.<sup>40</sup> Companies wishing to exclude a proposal must explain why in a written submission to the SEC staff, and shareholder proponents may (but need not) submit a response. The staff then responds to the request via a no-action letter. These no-action letters become the precedent for excluding, or not excluding, proposals under the rule. In addition, the staff occasionally may present its current thinking on discrete matters related to Rule 14a-8 through staff legal bulletins.<sup>41</sup> Our members generally have expressed frustration with this process, noting that the staff applies varying standards and reaches inconsistent judgments when determining if certain exclusions are available. We imagine this process also is challenging for the staff. We therefore encourage the Commission to review the current process and consider how it can be improved. For example, the SEC itself could propose and adopt guidance on certain matters. Commission guidance would provide a foundation to enhance consistency and be in accord with Chairman Clayton's views about staff guidance generally.<sup>42</sup>

<sup>40</sup> "Relevance" provides a ground for exclusion "[i]f the proposal relates to operations which account for less than 5 percent of the company's total assets at the end of its most recent fiscal year, and for less than 5 percent of its net earnings and gross sales for its most recent fiscal year, and is not otherwise significantly related to the company's business." "Management functions" (or "ordinary business") provides a ground for exclusion "[i]f the proposal deals with a matter relating to the company's ordinary business operations." "Conflicts with company's proposal" provides a ground for exclusion "[i]f the proposal directly conflicts with one of the company's own proposals to be submitted to shareholders at the same meeting." "Substantially implemented" provides a ground for exclusion "[i]f the company has already substantially implemented the proposal."

<sup>41</sup> See, e.g., SEC Staff Legal Bulletin No. 14I (Nov. 1, 2017), available at [www.sec.gov/interps/legal/cfslb14i.htm](http://www.sec.gov/interps/legal/cfslb14i.htm).

<sup>42</sup> Statement Regarding SEC Staff Views, SEC Chairman Clayton (Sept. 13, 2018) (stating that the "Commission's longstanding position is that all staff statements are nonbinding and create no enforceable legal rights or obligations of the Commission or other parties"), available at [www.sec.gov/news/public-statement/statement-clayton-091318](http://www.sec.gov/news/public-statement/statement-clayton-091318). Ms. Vanessa Countryman March 15, 2019 Page 17 VI. Proxy Voting Mechanics and Unique Concerns for Funds Both the Proxy Roundtable (which included a panel on proxy mechanics and technology) and Chairman Clayton's testimony addressed proxy plumbing issues. Below we make two important plumbing-related recommendations.

**A. Provide Ability to Confirm Votes Are Cast** As Instructed Regulated funds and other institutional investors have raised concerns regarding their inability to confirm whether their votes have been tabulated in accordance with their instructions. Our members attribute this difficulty to the complexity of the current process, its lack of transparency, or participants' unwillingness or inability to share voting information with appropriate parties. And yet, funds take great care in analyzing proposals and casting votes, which may be decisive on certain matters. Systemwide complexity and opacity is very much at odds with the importance that the Commission and market participants place on proxy voting. We therefore strongly recommend that the Commission consider pursuing a rule that would impose certain standardized requirements—with respect to information subject to confirmation and specified time frames—that issuers (or their

agents) must follow to confirm votes upon a shareholder's request. Such a rule would require that issuers have access to all information necessary to confirm votes to shareholders (or their agents). This would ensure that the confirmation process is the same without regard to the issuer or proxy, provide certainty regarding the timing of the confirmation process, and facilitate the SEC's ability to inspect compliance.<sup>43</sup> While any rule should include certain standardized baseline requirements, the Commission must be mindful of the complexity of any solution. Any rulemaking should support verification of voting, permit flexible alternatives to encourage competition and cost-effective solutions, and be technology-neutral to allow for future improvements.<sup>44</sup>

**B. Facilitate Regulated Funds' Ability to Communicate with Their Shareholders**

Omnibus accounts have become so pervasive that it can be difficult, if not impossible, for funds to communicate directly with large segments of their shareholders. Furthermore, trends in how shareholders prefer to communicate have exacerbated these difficulties, even when funds are able to identify them. For example, the transition away from landlines to cell phones has made it more challenging for funds to reach their shareholders at convenient times to solicit proxy votes. As a result, <sup>43</sup> We also strongly recommend that issuers be prohibited from providing vote confirmation information to anyone other than the requesting shareholder (or its agent). This would protect shareholders' privacy interests. <sup>44</sup> The Commission's experience with overseeing the NYSE's administration of processing fees for the delivery of proxy materials and other shareholder communications is instructive. In particular, it illustrates the importance of not creating a regulatory requirement that, by its nature, may inhibit competition. Ms. Vanessa Countryman March 15, 2019 Page 18 obtaining shareholder votes (including those required by statute) is quite challenging and expensive, for both legal and practical reasons. We therefore recommend that the SEC consider making the process for soliciting fund shareholder votes more efficient and less costly. One way the SEC could do this is by allowing funds to deliver their proxy materials directly to their shareholders. The SEC could require intermediaries to maintain and provide lists of all fund shareholders and their delivery preferences to funds, solely for distributing fund proxy materials, irrespective of their status as an "OBO" or "NOBO."<sup>45</sup> This practical and fair suggestion would improve funds' ability to communicate directly to their shareholders and lower their proxy solicitation costs.<sup>46</sup>

<sup>45</sup> The SEC has adopted rules that govern when an issuer may obtain a list of its "street name" shareholders who have not objected to such disclosure. These shareholders are "non-objecting beneficial owners," or "NOBOs," while "OBOs" are shareholders who have objected to the disclosure of their identities and share positions. Funds currently do not send fund materials to NOBOs directly because these NOBO lists lack needed information, and the NYSE-set fee for obtaining these lists is too high. And the NOBO list does not include OBOs, which represent the majority of intermediary-held accounts. <sup>46</sup> Funds could select their own vendor, negotiate a competitive price on behalf of fund shareholders, and then request a regulatory mailing list from the intermediary and provide it to the fund's selected vendor. Intermediaries already maintain the information that would be required in a regulatory mailing list. See Letter from Susan Olson, General Counsel, ICI, to Brent J. Fields, Secretary, SEC, regarding SEC Request for Comments on the Processing Fees Charged by Intermediaries for Distributing Materials Other Than Proxy Materials to Fund Investor (Oct. 31, 2018) (available at [www.sec.gov/comments/s7-13-18/s71318-4594882-176335.pdf](http://www.sec.gov/comments/s7-13-18/s71318-4594882-176335.pdf)) for additional information regarding how the SEC could accomplish this with respect to proxy and other regulatory materials. Ms. Vanessa Countryman March 15, 2019 Page 19 \* \* \* \* \*

ICI appreciates the opportunity to provide our views on how a reconsideration of the proxy voting regulatory regime will affect regulated funds and their shareholders. We stand ready to assist the SEC in any way as it moves forward with this initiative. If you have any questions, please contact me at 202- 326-5901, Susan Olson at 202-326-5813, Dorothy Donohue at

202-218-3563, or Matthew Thornton at 202-371-5406. Sincerely, /s/ Paul Schott Stevens  
Paul Schott Stevens President and CEO Investment Company Institute cc: The Honorable  
Jay Clayton The Honorable Robert J. Jackson, Jr. The Honorable Hester M. Peirce The  
Honorable Elad L. Roisman Dalia Blass, Director Paul Cellupica, Deputy Director and Chief  
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