

Legal Update

SEC Proposes To Rescind Recently Adopted Proxy Voting Advice Rules

The US Securities and Exchange Commission (the “SEC” or the “Commission”) proposed changes to the proxy solicitation rules on November 17, 2021. The proposed changes would rescind certain new rules adopted by the SEC in July 2020 (the “Adopted Rules”) that apply to proxy voting advice produced and disseminated by proxy advisory firms, otherwise known as proxy voting advisory businesses (“PVABs”).

Background

PVABs, such as Institutional Shareholder Services Inc. (“ISS”) and Glass, Lewis & Co., using their own benchmark recommendations or tailoring recommendations to a particular client’s request, provide advice to asset manager clients on how to vote on matters at public company shareholder meetings. In addition, some PVABs provide electronic platforms that not only deliver that advice, but also pre-populate client ballots for each applicable shareholder meeting and submit those votes to be counted (either after client review or automatically as soon as the recommendations are generated on the platforms). This advice and the vote submission service are valuable to the PVABs’ clients given that many asset managers invest in hundreds, if not thousands, of companies, many of which hold their annual shareholders’ meetings during the same time frame each year.

PVABs have historically been unregulated but are believed to influence a significant portion of shareholder votes on any given matter presented by a company or one of its shareholders. During the last administration, the SEC tackled the controversial issue of PVAB influence over proxy voting by revising the proxy solicitation rules to require that PVABs base their proxy voting advice on the most accurate information reasonably available and that PVABs be transparent regarding their conflicts of interest and the methodologies used to formulate their advice. For a fulsome explanation of the Adopted Rules, please refer to our Legal Update, “SEC Adopts Proxy Voting Advice Rule Amendments,” dated July 28, 2020,¹ which covers the Adopted Rules, as well as their history, in detail.

The Adopted Rules:

- amended Rule 14a-1(l) to codify the SEC’s longstanding position that voting advice provided by PVABs generally constitutes a solicitation under the proxy rules;
- amended Rule 14a-2(b) to add the following principles-based conditions to the exemptions to the information and filing requirements of the proxy rules that PVABs have historically relied on:

- PVABs must disclose conflicts of interest to their clients in their proxy voting advice or in the electronic medium used to deliver that advice;
- PVABs must establish procedures designed to allow all companies that are the subject of PVAB voting advice to have access to that advice in a timely manner; and
- PVABs must provide a mechanism for their clients to become aware of any written company response to their voting advice on a timely basis before they vote; and
- added to the examples of misleading information in Rule 14a-9 to make clear that the failure to disclose material information regarding proxy voting advice, such as a PVAB’s methodology, sources of information or conflicts of interest, could cause such advice to be misleading in violation of the proxy rules.

The adoption of these rules was not without controversy. ISS, possibly the largest PVAB subject to the Final Rules, filed a lawsuit against the SEC, challenging the Adopted Rules, as well as related Commission guidance. The amendments to Rules 14a-1(l) and 14a-9 became effective on November 2, 2020, although those revisions did not create any new obligations. Compliance with the conditions in Rule 14a-2(b) was not required until December 1, 2021. Upon taking office, SEC Chair Gensler directed the Staff to consider whether to recommend revising the Adopted Rules. On June 1, 2021, the SEC Staff published a statement announcing that it would not enforce the Adopted Rules or related guidance. The National Association of Manufacturers has since sued the SEC alleging a violation of the Administrative Procedure Act for refusing to enforce the Adopted Rules.

Proposal

On November 17, 2021, the Commission voted to propose to rescind certain of the Adopted Rules. Specifically, the Commission proposes to rescind the condition that would require PVABs to provide their proxy voting advice to subject companies and the condition that would require PVABs to alert their clients to any company response. In addition, the Commission voted to remove the example from Rule 14a-9, while affirming in the proposing release that a “PVAB, like any other person engaged in solicitation, may, depending on the facts and circumstances, be subject to liability under Rule 14a-9 for a materially misleading statement or omission of fact, including with regard to its methodology, sources of information or conflicts of interest.” The press release announcing the action explained the current Commission’s view that the Adopted Rules “may impede and impair the timeliness and independence of proxy voting advice and subject proxy voting advice businesses to undue litigation risks and compliance costs.”

Practical Considerations

The treatment of proxy voting advice for the purposes of proxy rules is a complex issue with divergent, and often-competing, views coming from various perspectives. However, proxy voting advice can influence proxy voting outcomes. Therefore, companies and other participants in the proxy process should monitor the proposal closely.

The public now has until December 27, 2021 to comment on the proposal. Given that short time period, interested parties should quickly determine whether they want to submit comments and, if so, begin drafting them immediately.

These proposed revisions, if adopted, are expected to have limited practical effect on the way in which PVABs are now doing business, because the rules proposed to be rescinded are not being enforced by the SEC.

Notably, the SEC did not propose to rescind the amendment that codified the definitions of the terms “solicit” and “solicitation” as including proxy voting advice. As a result, the proposal, if adopted, would not eliminate the requirement for PVABs, depending upon particular facts and circumstances, to disclose conflicts of interest. Therefore, to the extent any PVABs do not do so already, they may need to provide, or enhance the presentation of, conflict of interest information for their clients.

For more information about the topics raised in this Legal Update, please contact the author, Christina Thomas, or any of the following additional lawyers.

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ENDNOTES

¹ Available at <https://www.mayerbrown.com/-/media/files/perspectives-events/publications/2020/07/sec-adopts-proxy-voting-advice-rule-amendments.pdf>.

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