

Statement Announcing SEC Staff Roundtable on the Proxy Process

Chairman Jay Clayton
July 30, 2018

Shareholder engagement is a hallmark of our public capital markets, and the proxy process is a fundamental component of that engagement. In 2010, the Commission issued a concept release seeking public comment on whether the U.S. proxy system as a whole operates with the accuracy, reliability, transparency, accountability, and integrity that shareholders and companies should expect.[1] In light of the many changes in our markets, technology, and how companies operate since then, SEC staff will host a roundtable this fall to hear from investors, issuers, and other market participants about whether the SEC's proxy rules should be refined.

The SEC's rules governing the proxy process are at the center of investor participation in, and influence over, corporate governance at U.S. public companies. For example, our proxy rules specify the requirements for information companies must provide to shareholders and how votes may be solicited. Since the 2010 concept release, we have seen a dramatic increase in the number of U.S. companies reporting shareholder engagement, with 72% of S&P 500 companies reporting engagement with shareholders in 2017, compared to just 6% in 2010.[2] The scope of topics subject to shareholder engagement also has increased. Consistent with the Commission's mission, we must regularly review whether our existing rules are achieving their objectives effectively in light of changes in our marketplace. The SEC staff roundtable is intended to facilitate that type of assessment with respect to the proxy process and shareholder engagement.

SEC staff will announce the roundtable agenda items shortly. As they develop that agenda, I have asked that staff consider the topics outlined below.

Potential Topics for Consideration

Voting Process

Accuracy, transparency, and efficiency in the proxy system can inspire confidence in the proxy voting process for both companies and investors. Areas that may warrant particular attention include:

- Potential for over-voting and under-voting of securities by broker-dealers, the reasons this may occur, and ways to address it. In addition, the extent to which "empty voting" (e.g., acquiring voting rights over shares but having little or no economic interest in the shares) is of concern to market participants and the regulatory steps, if any, that should be taken to address those concerns.
- Practical difficulties in confirming whether an investor's shares have been voted in accordance with the investor's instructions. For example, challenges could be attributable to the number of participants that may be involved in the process, including issuers, transfer agents, third-party administrators, vote tabulators, securities intermediaries, and proxy service providers.
- Costs and challenges associated with distributing proxy and other materials to beneficial owners who hold in "street name," as well as the costs and other challenges of communicating with such shareholders more generally. In particular, concerns have been expressed about the ability and expense for issuers to communicate with street name holders through securities intermediaries, regardless of whether the shareholder is an "objecting beneficial shareholder" or "non-objecting beneficial shareholder."

Retail Shareholder Participation

In the 2017 proxy season, retail shareholders voted approximately 29% of their shares, while institutional investors voted approximately 91% of their shares.[3] In this regard, it may be useful

to better understand:

- Reasons for this relatively low retail participation rate and whether better communication and coordination among proxy participants, increased use of technology, changes to our rules, or investor education could increase participation.
- How 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. For example, some have suggested that fund shareholders should have a means of providing input into how the fund adviser votes its portfolio securities.
- And, more generally, the extent to which relatively low retail investor participation should be of concern and should inform analysis of existing regulation.

Shareholder Proposals

The shareholder proposal process is a channel for shareholders to engage with the U.S. public companies in which they invest on specific topics. All shareholders, as the ultimate owners of the company, bear the costs associated with management's consideration of a proposal and its inclusion in the proxy statement. And, those same shareholders may benefit from the engagement and potential for enhanced performance brought about by consideration of a shareholder proposal. Many market participants believe this dynamic has enhanced company performance. Many market participants also believe that the costs of this process could be significantly reduced without limiting (and potentially increasing) the benefits of shareholder engagement. In this vein, it often is noted that a small group of shareholders submits a significant percentage of the total number of shareholder proposals each year.[4]

Areas of the shareholder engagement process that may warrant particular attention include:

- Whether the current thresholds for minimum ownership (e.g., shares held and length of time) to submit a proposal to be included in the company's proxy statement[5] appropriately consider the interests of all shareholders, taking into account the potential benefits to shareholders of a proposal (or resubmission) being considered or adopted, as well as the costs associated with the inclusion of a proposal (or resubmission) in the proxy statement. Further, whether rules that allow companies to omit resubmitted proposals that received less than 3%, 6%, or 10% of the vote, depending on how many times the subject matter has been voted on in the last five years,[6] are appropriate.
- Whether meaningful ownership in the company can be demonstrated by factors other than the amount invested and the length of time shares are held.
- Whether the voices of long-term retail investors (who invest directly and indirectly through mutual funds, ETFs, and other products) are appropriately represented in the shareholder proposal process and in the shareholder engagement dynamic more generally.

Proxy Advisory Firms

Proxy advisory firms provide a number of services related to proxy voting, which include aggregating and standardizing information, providing platforms for managing votes, and providing voting recommendations. Areas that may warrant particular attention include:

- Whether various factors, including legal requirements, have resulted in investment advisers to funds and other clients relying on proxy advisory firms for information aggregation and voting recommendations to a greater extent than they should, and whether the extent of reliance on these firms is in the best interests of investment advisers and their clients, including funds and fund shareholders.
- Whether issuers are being given an appropriate opportunity to raise concerns if they disagree with a proxy advisory firm's recommendations, including, in particular, if the recommendation is based on erroneous, materially incomplete, or outdated information.

- Whether there is sufficient transparency about a proxy advisory firm’s voting policies and procedures so that companies, investors, and other market participants can understand how the advisory firm reached its voting recommendations on a particular matter, and whether comparisons of recommendations across similarly situated companies have value.
- Whether there are conflicts of interest, including with respect to related consulting services provided by proxy advisory firms, and, if so, whether those conflicts are adequately disclosed and mitigated.
- The appropriate regulatory regime for proxy advisory firms and whether prior staff guidance about investment advisers’ responsibilities in voting client proxies and retaining proxy advisory firms[7] should be modified, rescinded, or supplemented.

Technology and Innovation

The use of technology is implicated in all areas of the proxy process. As such, it may be appropriate to consider the following:

- As technology continues to evolve, whether it can be used to make the proxy process more efficient and effective for participants.
- The potential benefits and consequences that could result from further reliance on, and changes in, technology. For example, whether technology, such as “blockchain” or distributed ledger technology, could be used to streamline or create more accountability in the proxy process.

Other Commission Action

In 2016, the Commission proposed amendments to the proxy rules to require the use of universal proxy cards that would include the names of all nominees in contested board of directors’ elections.[8] Under existing rules, nominees must consent to including their names on a proxy card. This means that in an election contest, a dissident may not include the other party’s nominees unless it receives consent, which in my experience has rarely been provided. A consequence of this current rule is that, if a shareholder wants to vote for a combination of directors (e.g., some from the management slate and some from the dissident slate), he would have to attend the shareholder meeting in person.

Roundtable Details

The roundtable date, agenda items, panelists, moderators, and logistical information will be made public as they are finalized.

Members of the public who wish to provide their views on the proxy process, either in advance of or after the roundtable, may submit comments electronically or on paper.[9] Please submit comments using one method only. Information that is submitted will become part of the public record of the roundtable and posted on the SEC’s website. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make publicly available.

Electronic Comments:

- Use the SEC’s Internet submission form or send an email to rule-comments@sec.gov .

Paper Comments:

- Send paper comments to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, D.C. 20549-1090.
- All submissions should refer to File Number 4-725, and the file number should be included on the subject line if email is used.

Endnotes

[1] Concept Release on the U.S. Proxy System, Release No. 34-62495 (July 14, 2010) [75 FR 42982 (July 22, 2010)]. The comment letters received in response to the 2010 concept release are available at <https://www.sec.gov/comments/s7-14-10/s71410.shtml>.

[2] See Ernst & Young 2017 Proxy Season Review (June 2017), available at [https://webforms.ey.com/Publication/vwLUAssets/ey-2017-proxy-season-review/\\$File/ey-2017-proxy-season-review.pdf](https://webforms.ey.com/Publication/vwLUAssets/ey-2017-proxy-season-review/$File/ey-2017-proxy-season-review.pdf).

[3] See ProxyPulse, 2017 Proxy Season Review (September 2017), available at <https://www.pwc.com/us/en/governance-insights-center/publications/assets/pwc-proxypulse-2017-proxy-season-review.pdf>.

[4] See Gibson Dunn, Shareholder Proposal Developments During the 2018 Proxy Season (July 12, 2018), available at <https://www.gibsondunn.com/wp-content/uploads/2018/07/shareholder-proposal-developments-during-the-2018-proxy-season.pdf> (one proponent, and shareholders associated with him, submitted or co-filed 24% of all proposals in the 2018 proxy season).

[5] Shareholders must own either \$2,000 or 1% of a company's stock for one year. 17 CFR 240.14a-8(b).

[6] 17 CFR 240.14a-8(i)(12).

[7] See SEC Staff Legal Bulletin No. 20, Proxy Voting: Proxy Voting Responsibilities of Investment Advisers and Availability of Exemptions from the Proxy Rules for Proxy Advisory Firms (June 30, 2014); Institutional Shareholder Services, Inc. SEC Staff Letter (Sept. 15, 2004); Egan-Jones Proxy Services, SEC Staff Letter (May 27, 2004). The guidance states that investment advisers should ascertain whether a proxy advisory firm has the capacity and competency to adequately analyze proxy issues, including the robustness of its policies and procedures identifying and addressing any conflicts of interest. In addition, the guidance addressed the availability and requirements of two exemptions from the federal proxy rules that are often relied upon by proxy advisory firms. SEC Staff Legal Bulletin No. 20 (June 30, 2014).

[8] Universal Proxy, Release No. 34-79164 (October 16, 2016) [81 FR 79122 (November 10, 2016)]. The comment letters received in response to the 2016 proposing release are available at <https://www.sec.gov/comments/s7-24-16/s72416.htm>.

[9] Comments on the use of universal proxy cards should be submitted to the rulemaking file for the 2016 Universal Proxy release using the Commission's Internet comment form (<http://www.sec.gov/rules/proposed.shtml>) or via email to rule-comments@sec.gov (please include File Number S7-24-16 on the subject line).