



CENTER FOR CAPITAL MARKETS  
C O M P E T I T I V E N E S S

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February 18, 2015

The Honorable Mary Jo White  
Chair  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Re: Roundtable on Proxy Voting

Dear Chair White:

The U.S. Chamber of Commerce<sup>1</sup> (“Chamber”) created the Center for Capital Markets Competitiveness (“CCMC”) to promote a modern and effective regulatory structure for the capital markets to fully function in a 21<sup>st</sup> century global economy. It is an important priority of the CCMC to advance an effective and transparent corporate governance system that encourages shareholder communications and participation.

We would like to thank the Securities and Exchange Commission (“SEC” or “Commission”) for holding the upcoming roundtable on proxy voting. However, the CCMC is concerned that a universal ballot is a vehicle to fix the unbroken. Consequently, the universal ballot will divorce corporate governance from the fiduciary duties integral to the long-term performance of a public company and its ability to provide a return to investors. Director elections will turn into annual political-style campaigns and create dynamics that are not conducive to the effective management of a public company.

The SEC has also, through benign neglect, ignored the needs of retail shareholders, which has led to their increasing disenfranchisement in the proxy voting process. This has created an uneven playing field that distorts and harms the proxy voting system and fails to ensure reasonable and balanced corporate governance

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<sup>1</sup> The Chamber is the world’s largest business federation, representing the interests of more than 3 million businesses and organizations of every size, sector, and region.

policies that benefit companies and their investors, and which keep American capital markets from reaching their competitive potential in a global economy.

Starting in 2009, the CCMC has written to the SEC on numerous occasions proposing solutions to enfranchise retail shareholders.<sup>2</sup> To redress imbalances in the proxy voting system and provide retail shareholders with the same privileges as large shareholders, the CCMC respectfully requests that the SEC:

- 1. Examine possible interpretive guidance to give retail shareholders access to Client Directed Voting;**
- 2. Encourage greater use of web-based communications and technology; and**
- 3. Streamline proxy disclosures through the SEC's Disclosure Effectiveness Project.**

Each of these policies are interrelated and it is important that all of these steps be taken together to boost retail shareholder participation in director elections and consideration of shareholder proposals.

Our concerns and suggestions are discussed in greater detail below.

### **Discussion**

In 2009, the Chamber developed principles, crafted in consultation with businesses and investors, which should be incorporated into effective corporate governance and executive compensation policies. These principles, in our view, should guide appropriate policy making related to corporate governance, investor responsibility and executive compensation:

- Corporate governance policies must promote long-term shareholder value and profitability but should not constrain reasonable risk-taking and innovation.**

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<sup>2</sup> See letters from the CCMC to SEC Chairman Mary Schapiro, September 16, 2009; CCMC Comment Letter on the Proxy Voting System Concept Release, September 20, 2010; CCMC Comment Letter on the Proxy Voting System Concept Release, November 1, 2012; and CCMC Comment Letter on Proposed Rule Change to amend New York Stock Exchange Rule 451 and 465.

- **Long-term strategic planning should be the foundation of managerial decision-making.**
- **Corporate executives' compensation should be premised on a balance of individual accomplishment, corporate performance, adherence to risk management and compliance with laws and regulations, with a focus on shareholder value.**
- **Management needs to be robust and transparent in communicating with shareholders.**

These principles provide a template for policies that will allow for reasonable risk taking, continued innovation, the ability to acquire and retain talent and the protection of investor rights. We believe that these principles should be the touchstone for the consideration of the universal ballot, as well as common sense reforms for retail shareholders.

**a. Universal Ballot**

For decades, SEC rules have allowed a shareholder who is willing to commit the necessary resources to conduct a proxy contest to seek a change in board composition. If such a shareholder is able to nominate credible, qualified candidates that garner the widespread support of other investors, the shareholder can, in fact, alter the make-up of the board. With these rules already in place, we do not see a compelling reason to change what is not broken.

Mandating a universal ballot, also known as a universal proxy card, at all public companies would inevitably increase the frequency and ease of proxy fights. Such a development has no clear benefit to public companies, their shareholders, or other stakeholders. The SEC has historically sought to remain neutral with respect to interactions between public companies and their investors, and has always taken great care not to implement any rule that would favor one side over the other. We do not understand why the SEC would now pursue a policy that would increase the regularity of contested elections or cause greater turnover in the boardroom.

A board of directors has a fiduciary duty to act in the best interests of a corporation and its shareholders. A board is also accountable to the company's

shareholders through the company's charter, bylaws and corporate governance policies, as developed within the context of state incorporation statutes and federal securities laws. Instead of this system of accountability, the universal proxy card would facilitate proxy fights by individual shareholders (or small groups of shareholders) who do not have a similar fiduciary duty, are not bound by the company's corporate governance policies, and who may nominate directors who advance their own parochial agenda without regard to the broader best interests of the company or its shareholders. In striking down Rule 14a-11 (the SEC's mandatory proxy access rule), the D.C. Circuit cited the SEC's failure to assess the risk of giving special interest groups new powers to pursue self-interested objectives rather than the goal of maximizing shareholder value.<sup>3</sup>

Proxy contests are significantly disruptive to public companies, often to the ultimate detriment of their investors.<sup>4</sup> Promoting proxy contests should not be a goal of the SEC, as boards of directors would be increasingly forced to focus a company's resources in support of board-nominated candidates, detracting from managing and overseeing company business. The constant churning of directors could lead to the formation of factions on the board of directors, resulting in balkanization of the board. A politicized board cannot effectively serve the long-term best interests of investors or other corporate constituencies.

Indeed, the universal ballot may empower a small vocal minority at the expense of the majority. This clearly was a major concern of the court in striking down the SEC's Proxy Access rule.<sup>5</sup>

Seeking to avoid the cost and distraction of an SEC-sanctioned proxy fight, many companies will simply follow the path of least resistance and negotiate to place dissident directors directly on their boards without the need for a shareholder vote. This phenomenon will serve to further accelerate the pace at which activists pursue board representation in what becomes a vicious cycle. Again, the winner here is the special interest activist—not the rank-and-file investor.

Many advocates for the universal proxy card invariably cite the concept of advancing "corporate democracy." The reality is that the two dominant proxy advisory firms—firms that own no stock and owe no duties to American

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<sup>3</sup> See *Business Roundtable & U.S. Chamber of Commerce v. SEC*, 647 F.3<sup>rd</sup> 1144 (D.C. Cir. 2011).

<sup>4</sup> See Chamber August 14, 2009 comment letter on Facilitating Shareholder Director Nominations, File No. S7-10-09.

<sup>5</sup> See *Business Roundtable & U.S. Chamber of Commerce v. SEC*, n.3, *Supra*.

shareholders, employees or consumers—have come to exert an inordinate influence on the casting of votes at U.S. public companies. The lack of transparency, the one-size-fits-all policies, and the routine mistakes and the rampant conflicts of interest at proxy advisory firms are well-documented. We believe the SEC has started to take the first steps to address these issues through the release of SEC staff guidance on proxy advisory firms.<sup>6</sup> However, as we enter the first proxy season since its release, it is too early to know if the SEC staff guidance is sufficient to address these issues or if more needs to be done.

Despite all these flaws in the governance and regulation of proxy advisors, movement to the universal proxy card would further expand the influence of proxy advisory firms and thereby cement their grasp on corporate governance of public companies. A system in which one or two actors control the outcome of an election is no kind of democracy at all.

We see little reason to reimagine a process that, by and large, has served public companies and their investors well for decades. The current system of proxy voting for directors is well-understood by the marketplace and has been the basis for tens of thousands of orderly director elections (including countless proxy contests) over many, many years. More fundamentally, the proxy contest should be the last resort in corporate governance, not the first. Rather, robust communications between management and shareholders should continue to be the preferred mechanism to resolve issues.

#### **b. Retail Shareholder Issues**

Retail shareholders generally invest in companies with an interest in attaining long-term growth. Cumbersome voting procedures combined with dense disclosures have driven retail shareholder participation in corporate elections to historic lows, sometimes with participation rates below 10%. By contrast, many large institutional investors are mandated to participate in corporate elections by law or regulation. These institutional investors can use a variety of tools to help streamline their voting and due diligence processes, making possible significant levels of participation. Unfortunately, retail shareholders do not have similar options.

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<sup>6</sup> See *Proxy Voting: Proxy Voting Responsibilities of Investment Advisors and Availability of Exemptions from the Proxy Rules for Proxy Advisory Firms*, released by the SEC on June 30, 2014.

This situation has created an imbalance where institutional and activist investors must vote and have the means necessary to facilitate this process, yet retail shareholders are not given access to a similar array of tools. Concurrently, some large activist institutional investors obtain stakes in a company to further short-term objectives through their shareholder franchise. Other special interest activists may use the corporate governance system not as a means to ensure reform but rather to push an agenda unrelated to shareholder interests.<sup>7</sup> These objectives frequently have no relation to securing long-term shareholder returns. This inequity in shareholder rights erodes confidence in, and the credibility of, the corporate election system, undermining the SEC's mission to protect the rights of all investors.

While some small halting measures, such as the Financial Industry Regulatory Authority ("FINRA") and New York Stock Exchange ("NYSE") rule changes allowing greater use of enhanced broker internet platforms, have sought to address these issues, the languishing of the proxy voting systems concept release is testament to the inactivity on retail shareholder issues.

### **1. Examine Possible Interpretive Guidance to give Retail Shareholders Access to Client Directed Voting**

The Client Directed Voting model ("CDV") has emerged as a response to low retail shareholder participation. While there are many formulations of CDV, all involve a process by which a retail shareholder can provide some form of advance voting instructions to an entity authorized to vote his or her shares, subject to the shareholder's ability to change the instructions, or to override them on a case-by-case basis. Adoption of the CDV model would decrease the time and other costs of retail participation in the proxy voting process, allowing retail shareholders to establish standing instructions in accordance with their overall investment philosophy and strategy and to focus research and analysis on individual companies or proxy proposals that warrant individual attention. CDV would also be relatively easy to implement in tandem with enhanced broker internet platforms. .

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<sup>7</sup>Research conducted by the Manhattan Institute indicates that union pension funds tend to introduce more shareholder proposals at companies that are the ongoing targets of union-organizing campaigns. In 2012, for example, companies in lightly-unionized and labor-targeted sectors received significantly more shareholder proposals backed by employee pension funds than companies in other industries. James R. Copland, Op-Ed, *Manhattan Moment: Unions Target Corporations Through Shareholder Activism*, Wash. Examiner (July 19, 2012), available at <http://www.washingtonexaminer.com/manhattan-moment-unions-target-corporations-through-shareholder-activism/article/2502610>.

Allowing the use of a CDV model would give retail shareholders access to mechanisms used by other large institutional shareholders. This innovative change could allow for greater retail shareholder involvement in corporate elections and long-term decision making processes for companies. This will create a level of fairness and equal representation that is currently lacking in the corporate election process.

## **2. Encourage Greater Use of Web-Based Communications and Technology**

To further complement the CDV model and enhanced broker internet platforms, we recommend policies that more generally encourage broader use of technology to increase retail shareholder participation in the proxy voting process. In particular, greater use of virtual meetings would permit a greater number of shareholders to actively participate in the annual meetings of companies, where participation in physical meetings is impractical, as is often the case for retail shareholders.

## **3. Streamline Proxy Disclosures through the Disclosure Effectiveness Project**

Over the years since the securities laws were enacted, public company disclosures have become increasingly voluminous and complex, making it difficult for even the most sophisticated of investors to determine the most salient information about a company.<sup>8</sup> Retail investors are particularly vulnerable when our corporate disclosure regime makes it more difficult for them to make well-informed investment and voting decisions. This is hardly an environment that promotes retail investor participation in corporate governance.

The SEC's ongoing Disclosure Effectiveness Project provides the Commission with an opportunity not just to make company filings more intelligible, but to help retail investors become more involved in the governance of companies they invest in. The Commission should first take the step of eliminating outdated or duplicative information in filings, and then focus on more fundamental changes to a system that

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<sup>8</sup> A survey of 64 asset managers, conducted in the fall of 2014 and recently released by the Rock Center for Corporate Governance at Stanford University, Equilar and R.R. Donnelley, found that institutional investors also favor streamlined and simpler disclosures. Survey can be found here: [http://www.gsb.stanford.edu/sites/gsb/files/publication-pdf/cgri-survey-2015-deconstructing-proxy-statements\\_0.pdf](http://www.gsb.stanford.edu/sites/gsb/files/publication-pdf/cgri-survey-2015-deconstructing-proxy-statements_0.pdf)

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has been in place since the 1930's.<sup>9</sup> All investors—in particular retail investors—would then be able to make better informed investment and voting decisions.

### Conclusion

The public company model has fallen out of favor as a preferred mechanism for capital formation in this century. The SEC is at a crossroad and can engage in policy making that promotes the public company as an attractive investment vehicle for investors and incentivize competition in our capital markets, or make policy choices that continue the disfavor investors have shown through the allocation of capital in vehicles other than public companies.

As outlined, we have serious concerns in the consideration of the universal ballot—a response to a non-issue— which fails to promote the interests of a majority of shareholders. Similarly, we believe that the failure of the SEC to address issues related to retail shareholders has allowed serious shortcomings in the proxy voting system to worsen. As outlined in this and other letters, we believe there are common sense solutions that can be implemented to address these problems.

We look forward to continuing to work with the SEC on these important issues necessary to ensure that our proxy voting systems are fair, balanced, and help promote efficient capital markets that support public companies.

Sincerely,



Tom Quaadman

Cc: The Honorable Luis A. Aguilar  
The Honorable Daniel M. Gallagher  
The Honorable Kara M. Stein  
The Honorable Michael S. Piwowar  
Mr. Keith Higgins, Director, Division of Corporation Finance

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<sup>9</sup> In July 2014 the Chamber made a number of recommendations for the SEC's Disclosure Effectiveness project in a report entitled *Corporate Disclosure Effectiveness: Ensuring a Balanced System that Informs and Protects Investors and Facilitates Capital Formation*. The report can be found at: [http://www.centerforcapitalmarkets.com/wp-content/uploads/2014/07/CCMC\\_Disclosure\\_Reform\\_Final\\_7-28-20141.pdf](http://www.centerforcapitalmarkets.com/wp-content/uploads/2014/07/CCMC_Disclosure_Reform_Final_7-28-20141.pdf)