



November 5, 2018

Mr. Brent Fields  
Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Sent via e-mail ([rule-comments@sec.gov](mailto:rule-comments@sec.gov))

Dear Mr. Fields:

The Biotechnology Innovation Organization (BIO)<sup>1</sup> is pleased to submit comments to the Securities and Exchange Commission (SEC) on the upcoming roundtable on the proxy process, to be held on November 15. BIO applauds the SEC for its attention to the proxy plumbing system, in particular how the regulation of proxy advisory firms impacts U.S. public companies and their investors.

Emerging biotech companies working on innovative therapeutics are highly dependent on investment capital. More than 95% of these companies are in the R&D process without an FDA-approved product on the market. It costs over \$2.6 billion to develop a single life-saving treatment<sup>2</sup>, and most companies spend more than a decade in the lab before their first therapy is approved. During this long development process, virtually every dollar spent by an emerging biotech comes directly from investors, because biotechs remain pre-revenue through their entire time in the lab and the clinic. In short, investment capital is the lifeblood of scientific advancement. This unique business model underscores the importance of a strong relationship between biotechnology innovators and their investors. Accordingly, we have concerns about the role of proxy advisory firms in issues that impact our investors.

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<sup>1</sup> BIO is a not-for-profit trade association that represents approximately 1,000 biotechnology companies, academic institutions, state biotechnology centers, and related organizations in all 50 states. BIO members are working toward groundbreaking cures and treatments for devastating diseases, developing technologies for advanced biofuels and renewable chemicals, and researching novel gene traits for identifying food sources that could help combat global hunger.

<sup>2</sup> BIO, "The Biotechnology Ecosystem: By the Numbers," <https://www.bio.org/toolkit/infographics/biotechnology-ecosystem-numbers>.

In particular, we are concerned with the outsized influence, opaque standards, one-size-fits-all recommendations, and conflicts of interest of proxy advisory firms. Just two firms—Glass-Lewis and Institutional Shareholder Services (ISS)—make up roughly 97% of the proxy advisory firm market. This effective duopoly enables proxy advisory firms to have an outsized influence on the proxy voting process, which has increasingly been felt in board rooms and shareholder meetings across the country. Institutional investors’ reliance on proxy firms, combined with an overall rise in shareholder activism, has dramatically increased the firms’ ability to influence proxy votes and company decisions. One study found that opposition by a proxy advisor resulted in a 20% increase in votes cast in line with that recommendation, while another study found that a negative vote recommendation by ISS on a management proposal can result in a 13.6% to 20.6% sway in the vote.<sup>3</sup> ISS and Glass Lewis wield such power in the proxy process that emerging biotech companies have a very difficult time getting proposals approved if the proxy advisory firms oppose the resolution. Still, the proxy advisory firms are not held accountable for the accuracy, reliability or transparency of their recommendations.

Proxy advisory firms utilize specific methodologies to formulate voting recommendations, but companies and investors have no insight into those secret formulas (unless, in some circumstances, they pay consulting fees to obtain them). Without basic standards for transparency, companies are left in the dark with no ability to predict how the proxy advisory firms will approach a proxy proposal. We encourage the SEC to hold the proxy advisory firms to appropriate standards for transparency and accountability, including a requirement to disclose the policies and methodologies that they use to formulate voting recommendations, including how they consider the size of the company when making proxy voting recommendations.

Biotech companies have unique business models that are often disregarded by proxy advisory firms. Instead, the proxy advisory firms issue one-size-fits-all recommendations, and issuers do not have an opportunity to correct material errors or incomplete analysis in the data underpinning their voting recommendations. For instance, executive compensation packages for biotech companies often include deferred compensation provisions tied to the company’s performance in clinical trials, the outcome of which are central to the firm’s valuation. However, proxy voting recommendations on executive compensation packages are based on vague, opaque standards—such as that deferred comp should be tied to quarterly earnings—which is fundamentally misaligned with the business models of early-stage biotech companies. In this example, the influence of proxy advisory firms, coupled with one-size-fits-all recommendations, make it exceedingly difficult for small companies to attract and retain the talent necessary to advance their science, and investment advisors rely on recommendations that may not be in the shareholders’ best interest. Such one-size-fits-all standards undermine the reliability of proxy voting recommendations and the integrity of the voting process.

The conflicts of interest inherent in ISS’s business model and Glass Lewis’s ownership structure should be addressed. ISS’s consulting service charges public companies a fee to

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<sup>3</sup> [http://www.shareholderforum.com/access/Library/20130510\\_Larcker-McCall-Ormazabal.pdf](http://www.shareholderforum.com/access/Library/20130510_Larcker-McCall-Ormazabal.pdf)

learn how to best comply with its voting policies and obtain favorable recommendations in the future, and Glass Lewis's ownership structure has the potential to bias their recommendations particularly on activist shareholder proposals. The current design of the proxy voting process presumes that investment advisors rely on *independent* third parties, but because of these conflicts of interest, the two dominant proxy advisory firms are anything but independent. We encourage the SEC to require better transparency and disclosure of such conflicts, as well as hold the proxy advisory firms accountable to mitigate those concerns.

We applaud the SEC for withdrawing the no-action letters originally issued in 2004 to Egan-Jones Proxy Services and ISS. We encourage the SEC to build upon this step by reviewing and updating Staff Legal Bulletin No. 20 to provide further clarity on the responsibility that proxy advisory firms and their clients have to ensure that the proxy advisory firms: (i) have the competence to adequately analyze proxy issues for the breadth and scope of companies and industries for which they provide voting recommendations, including small businesses and emerging growth companies; (ii) have policies and procedures in place that are sufficiently robust and transparent for developing such voting recommendations; and (iii) adequately identify, mitigate and disclose their conflicts of interest. We encourage the SEC to adopt sensible reforms to the proxy process in light of the roundtable discussion, particularly to mitigate proxy advisory firms' conflicts of interest, increase transparency in the development of their voting recommendations, and ensure that dissenting opinions can be heard in order to give investors a full and accurate understanding of issues as they cast their votes.

BIO looks forward to working with the SEC as it continues to improve the proxy process for companies and shareholders alike. We welcome the opportunity to share further insights on the impact of proxy advisory firms on small public companies during the upcoming SEC Roundtable on the Proxy Process on November 15, 2018. Please contact Lisa Schaefer, Director of Financial Services Policy [REDACTED] if we can provide any additional support or information.

Sincerely,



Lisa Schaefer  
Director, Financial Services Policy



Cameron Arterton  
Vice President, Tax Policy