November 13, 2018

The Honorable Jay Clayton
Chairman
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: Rule 14a-8 and Proxy Process Reform

Dear Chairman Clayton:

We, the undersigned investors, representing total assets under management of almost $570 billion, respectfully write to express our views about the importance and benefits of shareholder proposals and proxy voting, and to urge the Securities and Exchange Commission ("SEC") to maintain Rule 14a-8 (the "Rule") as is. We appreciate the opportunity to comment on these matters prior to the SEC's upcoming Roundtable on the Proxy Process on November 15.

We believe that the current rules and thresholds under Rule 14a-8 work well for investors and issuers, and should be maintained. Under Rule 14a-8, a company is required to include shareholder proposals from eligible shareholders in its proxy materials unless the proposals do not meet the eligibility and procedural requirements of the Rule or are subject to exclusion on other bases as set forth therein. Shareholders who rely on the Rule may submit only one proposal per corporate annual meeting and are required to have continuously owned at least $2,000 in market value, or 1%, of an issuer's outstanding voting securities for a year or more by the date the proposal is submitted.

Currently, there are a number of bases upon which a company may rely to exclude shareholder proposals, including the provision of the Rule that governs the resubmission of such proposals. Pursuant to this provision, if the proposal addresses substantially the same subject matter as another proposal that has been previously included in the company's proxy materials within the prior five (5) calendar years, the proposal may be excluded for any shareholder meeting held within three (3) calendar years of the last submission if the proposal received: less than (i) 3% of the vote on its first submission; (ii) 6% on the second; or (iii) 10% on the third.[1]

Critics of the benefits of shareholder proposals and the manner in which Rule 14a-8 has effectively governed the proposal process express various arguments purporting to justify unnecessary reforms and prohibitive requirements. These proposed new requirements would restrict shareholders' ability to put forth and vote on important proposals. However, the arguments used to justify these new restrictions do not withstand scrutiny.

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[1] 17 C.F.R. § 240.14a-8(i)(12).

Shareholder Proposals Should Remain Open to Investors of All Sizes

Some critics argue that the SEC makes it too easy for shareholders to submit a proposal. Currently, a shareholder owning $2,000 worth of a company's shares for at least one year is permitted to submit a shareholder proposal. While at one time, ownership of a single share of stock came with the right to submit a proposal, in 1983 the SEC decided it made sense to have a modest but still low requirement, setting the threshold at $1,000 held for at least one year. The SEC in 1998 raised this to $2,000, "to adjust for the effects of inflation," but did not raise it further "in light of rule 14a-8's goal of providing an avenue of communication for small investors."

Such a requirement helps to ensure that smaller, 'Main Street' investors have the same rights to file a proposal as wealthier individuals and institutional investors. As such, the filing threshold ensures a form of shareholder democracy that is open to nearly all investors, as it should be.

Shareholder Proposals Cannot Currently be Re-submitted Too Easily

Critics of Rule 14a-8 suggest that resubmission thresholds should be raised to reduce the number of proposals filed repeatedly for a number of years. The data, however, do not support that re-filings are a problem. According to Institutional Shareholder Services ("ISS") data, from 2010 to 2017, shareholders resubmitted environmental and social issue proposals only 35 times after receiving votes under 20% for two or more years. This affected only 26 companies.[2] In other words, resubmission of proposals receiving less than 20% support for a third or fourth time is very rare. Moreover, the current resubmission thresholds create significant pressure on shareholder proponents and a higher threshold would put a high percentage of proposals at risk for exclusion from proxies. The ISS database tracked 459 shareholder proposals that went to a vote at Russell 3000 companies as of the third quarter of 2017. Of these proposals, 104 proposals (22.7%) received less than 10% of the For/Against vote. In comparison, 252 proposals (54.9%) received less than 30% of the For/Against vote.[3]

Experience indicates that it often takes several years for a proposal regarding an emerging issue to gain enough traction with investors to achieve double-digit votes. In many cases, these proposals eventually receive substantial support, leading to widespread adoption by companies.
For example, in 1987 an average of 16 percent of shareholders voted in favor of shareholder proposals to declassify boards of directors so that directors stand for election each year. In 2012, these proposals enjoyed an 81 percent level of support on average. Ten years ago, fewer than 40 percent of S&P 500 companies held annual director elections compared to more than two thirds of these companies today.[4] The current thresholds provide a reasonable amount of time for emerging issues to gain support among investors while ensuring that only those proposals that garner meaningful support remain on the ballot for multiple years.

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[2] ISS Voting Analytics database.

[3] Ibid.

[4] AFL-CIO letter to Stanford professors Larcker and Tayan, January 18, 2013

Shareholder Proposals are Not Abused by Activist Investors

Abuse of the proposal process by alleged activist investors is another misguided argument used in favor of restricting shareholders' rights. According to this allegation, a small number of activist investors abuse the system by accounting for a disproportionate volume of proposals. While the ISS database does show that the Chevedden, Steiner, and McRitchie families submitted 14.5% of the 11,706 proposals filed between 2004 and 2017, *the average vote on these proposals was 40%.*[5] This average vote level indicates that these filers provide a valuable service to fellow shareholders by promoting good corporate governance. For example, these investors frequently focus on encouraging companies to adopt best-practice corporate governance reforms such as eliminating supermajority voting requirements, appointing an independent board chair, eliminating staggered boards, and giving shareholders a "say on pay" and "proxy access" to nominate candidates for board elections.[6]

Shareholder Proposals Are Not the Cause of the Reduction in Public Traded Companies

Only a small proportion of proposals are filed at companies with a recent IPO -- less than 9% of Russell 3000 companies that have had an IPO since 2004 have received a shareholder proposal.[7] Because large companies make up a larger portion of investors' equity portfolios than small companies, larger companies are more likely to receive shareholder proposals. According to the ISS Voting Analytics database, S&P 500 companies received 659 proposals in 2017, which was equal to 77% of the 852 proposals that Russell 3000 companies received.[8] Moreover, only 3.7% of shareholder proposals in the ISS database were filed at companies with a market capitalization below $1 billion.[9]

There are numerous factors contributing to the reduction in the number of public companies in the U.S. According to Vanguard, these include:[10]

- a steep drop in the number of small and micro-firm IPOs compared with the number of IPOs during the tech bubble in the late 1990s. Vanguard explains: "It appears that companies are choosing to be acquired by larger public companies rather than go public themselves."
- In 2016, more than 4,800 private companies were acquired, compared with about 1,950 during the IPO peak in 1996.[11]
- Mergers are also the leading cause (and a generally growing proportion) of delistings.

[5] ISS Voting Analytics database.

[6] https://www.lexology.com/library/detail.aspx?g=b6ad9d24-4a68-4736-8b28-3bbbadfbd7f5

[7] ISS Voting Analytics database, and https://www.iccr.org/sites/default/files/resources_attachments/investor_response_to_chamber_14a-8_nov_9_final_2.pdf

[8] ISS Voting Analytics database.

[9] Ibid.

[10] https://personal.vanguard.com/pdf/ISGPCA.pdf

[11] https://www.ey.com/Publication/vwLUAssets/an-analysis-of-trends-in-the-us-capital-markets/$FILE/ey-an-analysis-of-trends-in-the-us-capital-markets.pdf

- Overall, Vanguard concludes that "the shrinking number of publicly listed companies consists almost entirely of those [micro] securities that would not have been invested in by active and passive funds anyway."

Vanguard also points out that growth in private equity is outpacing growth in public equity. Contributing to the growth in private funding of companies is a series of regulatory changes. The 1996 Securities Markets Improvement Act made it easier for private companies to sell stock to "qualified purchasers," meaning institutional investors and wealthy individuals.[12] In 2012 Congress boosted the allowed number of investors in large private firms from 500 to 2,000. The SEC also adopted rules to encourage "private placements," allowing private firms to raise millions of dollars while avoiding public reporting.[13] In addition, the growth in investment by mutual funds in late-stage private start-ups is providing resources that help companies delay going public.[14]

Due to these factors, among other macro forces such as low interest rates spurring debt financing,[15] private assets under management grew from less than $1 trillion in 2000 to more than $5 trillion last year. As a result, many companies no longer need an IPO to raise capital.[16]

At the same time, Wall Street fees for small company IPOs tend to be far higher than those paid by large companies. For example, Facebook paid around 1.1%, whereas many small companies pay roughly 7%.[17] SEC Commissioner Jackson labels these fees a "middle-market tax."[18]

These changes in market structure, and the deregulation of private investments, are far more important than shareholder proposals in reducing the number of public companies and offerings. In fact, there is no evidence that shareholder proposals are a factor in reducing IPOs, or in increasing the number of mergers, or companies going private.[19]

Shareholder Proposals Do Not Meaningfully Increase Costs

Most public companies do not receive any shareholder proposals. On average, 13% of Russell 3000 companies received a shareholder proposal in a particular year between 2004 and 2017 according to the ISS database.[20] In other words, the average Russell 3000 company can expect to receive a proposal once every 7.7 years. For companies that receive a proposal, the median number of proposals is one per year.

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[12] https://www.theatlantic.com/magazine/archive/2018/11/private-inequity/570808/

[13] Ibid.

[14] https://corpgov.law.harvard.edu/2017/09/28/the-evolution-of-the-private-equity-market-and-the-decline-in-ipos/ and https://www.ey.com/Publication/vwLUAssets/an-analysis-of-trends-in-the-us-capital-markets/$FILE/ey-an-analysis-of-trends-in-the-us-capital-markets.pdf

[15] Ibid.

[16] Ibid.

[17] https://www.theatlantic.com/magazine/archive/2018/11/private-inequity/570808/

[18] Ibod.

[19] https://www.iccr.org/sites/default/files/resources_attachments/investor_response_to_chamber_14a-8_nov_9_final_2.pdf, p. 10

[20] Ibid.

Importantly, the cost to companies of the existing shareholder proposal process is generally low (and something companies have control over managing),[21] and the process often results in benefits to companies. As noted, most companies receive few, if any, shareholder proposals. In 2016, there were fewer than 1,000 total shareholder proposals filed at all reporting companies in the U.S.[22] Only half of the proposals submitted by shareholders appear in companies' proxies and, consequently, relatively few companies (fewer than 500 in 2016) held votes on issues submitted by shareholders.[23] This is in part due to meaningful dialogues that happen between investors and management that leads to win/win agreements - resulting in the withdrawal of resolutions. In any given year one quarter to one third of resolutions on environmental and social issues, for example, are withdrawn because of such agreements. And some governance issues like majority vote for directors and access to the proxy result in even higher rates of agreement, making a vote unnecessary.

Finally, the SEC oversees a robust "no-action letter" process that allows companies to exclude proposals from the proxy ballot that do not meet specific procedural or substantive hurdles.

Investors Benefit from the Valuable Services Proxy Advisors Provide to Advance Good Corporate Governance

Some argue that investors over-rely on proxy advisors ISS and Glass Lewis who account for 97% of market share in the industry. The alleged result is that ISS and Glass Lewis functionally control substantial voting shares of thousands of companies in their portfolios, and that this control empowers them to set standards for corporate governance by choosing which shareholder proposals to support.

In fact, while many institutional investors do rely on proxy advisors for advice and administrative help, voting decisions remain the ultimate responsibility of investors. As CII states in their letter to the House Committee on Financial Services, dated Nov 9, 2017:

> *"Indeed, many pension funds and other institutional investors contract with proxy advisory firms to review their research, but most large holders have adopted their own policies and employ the proxy advisory firms to help administer the voting of proxies during challenging proxy seasons.*
>
> *In short, most large institutional investors vote their proxies according to their own guidelines. While large institutional investors rely on proxy advisors to manage the analysis of issues presented in the proxy statements accompanying over 38,000 meetings annually, and to help administer proxy voting, this does not mean that they abdicate their responsibility for their own voting decisions.*

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[21] The Dangerous "Promise of Market Reform": No Shareholder Proposals, Harvard Law School Forum on Corporate Governance and Financial Regulation, Adam Kanzer, 2017

[22] ISS Voting Analytics database.

[23] Ibid.

The independence that shareowners exercise when voting their proxies is evident in the statistics related to "say on pay" proposals and director elections. Although Institutional Shareholder Services Inc. (ISS), the largest proxy advisory firm, recommended against say on pay proposals at 11.92 percent of Russell 3000 companies in 2017, only 1.28 percent of those proposals received less than majority support from shareowners.[24] Similarly, although ISS recommended votes in opposition to the election of 10.43 percent of director-nominees during the most recent proxy season, just 0.185 percent failed to obtain majority support."[25]

<u>The Growth of Index Funds is Not Resulting in Too Much Power for Proxy Advisors</u>

Another complaint posits that passive fund managers of index funds do not have the time or incentive to obtain the necessary information about each company whose shares are owned in their funds to be well-informed voters. According to these critics, this problem is becoming more pressing with the growth of index funds. Nearly one-third of equity investment in the United States is via index funds, and index funds are the largest shareholders in 40% of public U.S. companies.[26] As a result, critics claim that passive fund managers' reliance on the advice of proxy advisors cedes shareholder power to, functionally, two firms. As index funds continue to account for more and more of equity ownership, proxy advisors will continue to obtain even more influence over shareholder proposals.

Again, the critics' argument assumes that passive fund managers blindly follow the recommendations of the proxy advisors. These managers almost always have detailed proxy voting guidelines that frequently result in a divergence between their votes and the recommendations of the proxy advisors. For example in 2017, BlackRock and Vanguard voted for 2% of all climate-related shareholder proposals tracked by the non-profit organization Ceres, including many proposals that proxy advisors recommended voting for.[27]

<u>Proxy Advisors Decrease Costs For Investors</u>

Reliance on proxy advisers provides cost savings and market externality benefits to investors. Large, widely diversified institutional investors must manage proxy voting related to up to 38,000 annual meetings globally each year according to CII. Clearly, it is more efficient for most investors to rely on assistance from proxy advisors who can spread some of the costs of voting across thousands of clients than for each institutional investor to try to manage this herculean ask on their own. CII's November 9th 2017 letter to House Financial Services Committee[28] noted that...

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[24] Ibid.

[25] ISS Voting Analytics Database (last viewed on Oct. 23, 2017 & on file with CII).

[26] Phil Gramm and Mike Solon, "Keep Politics Out of the Boardroom," WALL STREET JOURNAL, July 18, 2018.

[27] https://www.ceres.org/news-center/blog/four-mutual-fund-giants-begin-address-climate-change-risks-proxy-votes-how-about

[28] https://www.cii.org/files/issues_and_advocacy/correspondence/2017/Attachment%20to%20December%2012,%202017%20Letter.pdf

> *…in recent months the United States Department of Treasury (Treasury) performed outreach to identify views on proxy advisory firms in connection with its recently issued report to the President on "A Financial System that Creates Economic Opportunities, Capital Markets." In that report, the Treasury found that 'institutional investors, who pay for proxy advice and are responsible for voting decisions, find the services valuable, especially in sorting through the lengthy and significant disclosures contained in proxy statements.' More importantly, the Treasury did not recommend any legislative changes governing the proxy advisory firm industry.*[29]

Corporate Managers Benefit From Investor Input on Environmental, Social, and Governance Issues

One complaint argues that the shareholder proposal process is redundant because company management already considers environmental, social and governance (ESG) issues. However, if management already addresses a particular ESG issue set forth by the proposal, investors are far less likely to waste time filing the proposal in the first place, and the proposal can be challenged and rejected as "substantially implemented."

A second complaint concerns an alleged lack of connection between ESG issues and shareholder value. However, the Department of Labor has recognized that ESG issues can be significant:

> *[T]he Department merely recognized that there could be instances when otherwise collateral ESG issues present material business risk or opportunities to companies that company officers and directors need to manage as part of the company's business plan and that qualified investment professionals would treat as economic considerations under generally accepted investment theories. In such situations, these ordinarily collateral issues are themselves appropriate economic considerations, and thus should be considered by a prudent fiduciary along with other relevant economic factors to evaluate the risk and return profiles of alternative investments. In other words, in these instances, the factors are more than mere tie-breakers. To the extent ESG factors, in fact, involve business risks or opportunities that are properly treated as economic considerations themselves in evaluating alternative investments, the weight given to those factors should also be appropriate to the relative level of risk and return involved compared to other relevant economic factors.*[30]

In addition, investors such as BlackRock, State Street and more than 1,700 members of the Principles for Responsible Investment have all publicly proclaimed the importance of ESG issues

[29] U.S. Department of the Treasury, "A Financial System that Creates Economic Opportunities, Capital Markets" 31 (Oct. 7, 2017), https://www.treasury.gov/press-center/press-releases/Documents/A-Financial-System-CapitalMarkets-FINAL-FINAL.pdf.

[30] Field Assistance Bulletin 2018-01

to shareholder value.[31] These claims are backed by a robust set of academic research.[32,33] In fact, more than 20% of assets under management in U.S. markets are managed with some form of ESG strategy according to US SIF.[34] Clearly, ESG issues are frequently financially material.

The third and final concern relates to shareholder proposals that are redundant or overlap in content with other proposals filed with same company. In these cases, the SEC already serves as an impartial arbiter using specific guidelines. Under the existing Rule's framework, a company may request to exclude a shareholder proposal that (i) directly conflicts with one of the company's own proposals to be submitted to shareholders at the same meeting; (ii) the company has already substantially implemented the proposal; and (iii) if 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.

* * * * *

We do not believe revision of Rule 14a-8 is necessary at this time. The existing Rule currently allows institutional investors of all sizes and individual shareholders alike to engage corporate boards and senior management on their need to address important environmental, social, and governance issues and long-term risk management. Shareholder proposals frequently address emerging systemic risks to the U.S. and globally economies, such as the predatory lending that contributed to the 2008 financial crisis.

The current process also allows investors to communicate with boards, management, and other shareholders about the most effective, proactive way to protect investor interests with respect to corporate governance, risk, and policy issues affecting companies prior to a crisis.

As such, the existing process serves an important self-regulatory function for U.S. capital markets, allowing shareholders a means to protect their interests through a form of shareholder democracy. Additional government interference in this private ordering process is not necessary or advisable.

For these reasons, we oppose further restricting shareholder proposals, which are helpful to companies, investors, and the economy as whole. Thank you for considering these views. We welcome the opportunity to work with you to address these concerns.

Sincerely,

Addenda Capital
Adrian Dominican Sisters, Portfolio Advisory Board
Bailard, Inc
Bon Secours Mercy Health

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[31] https://www.unpri.org/pri/what-are-the-principles-for-responsible-investment

[32] https://responsiblebusiness.haas.berkeley.edu/research/moskowitz-past-winners.html

[33] https://www.ussif.org/performance

[34] https://www.ussif.org/files/SIF_Trends_16_Executive_Summary(1).pdf

Boston Common Asset Management
CCLA Investment Management
Christopher Reynolds Foundation
Committee on Mission Responsibility Through Investment of the Presbyterian Church U.S.A.
Congregation of St. Joseph
Connecticut Retirement Plans and Trust Funds
Daughters of Charity, Province of St. Louise
Dignity Health
Educational Foundation of America
Friends Fiduciary Corporation
Green Century Capital Management
Impax Asset Management LLC
Inherent Group, LP
Interfaith Center on Corporate Responsibility
Loring, Wolcott & Coolidge
Maryknoll Sisters
Maryland State Retirement and Pension System
Maryland State Treasurer
McKnight Foundation
Mercy Investment Services, Inc.
Miller/Howard Investments, Inc
Oregon State Treasury
Parametric
Parnassus Investments
Progressive Investment Management
Seattle City Employees' Retirement System
Seventh Generation Interfaith, Inc.
The Episcopal Church USA
Tri-State Coalition for Responsible Investment
Trillium Asset Management
Trinity Health
Unitarian Universalist Association
USA West Province of the Society of Jesus
Walden Asset Management / Boston Trust

Cc: Commissioner Robert J. Jackson, Jr.
Commissioner Hester M. Pierce
Commissioner Kara M. Stein
Commissioner Elad L. Roisman