



June 7, 2019

Vanessa Countryman  
Acting Secretary  
U.S. Securities Exchange Commission  
100 F Street, NE  
Washington, D.C. 20549-1090

**RE: File No. 4-725 Reforms to the U.S. Proxy System**

Ms. Countryman,

The American Securities Association (ASA) is submitting these comments in response to Chairman Clayton's initiation of a comprehensive review of the proxy process in late 2018.<sup>1</sup> We would like to commend the Chairman for initiating this process, and Commissioner Roisman for spearheading this effort. While many aspects of the U.S. proxy system are ripe for modernization, we believe that rulemakings to address the conflicts of proxy advisory firms and shareholder proposals under Exchange Act Rule 14a-8 are the most urgent priorities. Our thoughts on these issues are discussed below in greater detail.

**Reform Proxy Advisory Firms**

Proxy advisory firms are expected to provide *unbiased and expert* advice on shareholder proposals that are intended to maximize returns on investments. Unfortunately, two advisory firms, Glass Lewis and Institutional Shareholder Services (ISS), control an estimated 97 percent<sup>2</sup> of the market, providing them with outsized influence on voting recommendations and the ability to have a major impact on voting outcomes. These two firms also operate with significant conflicts of interest, provide little transparency into how they formulate voting recommendations, and often fail to produce company-specific analysis – instead relying on broad policy 'benchmarks' intended to apply to all public companies.

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<sup>1</sup> The ASA is a trade association that represents the retail and institutional capital markets interests of regional financial services firms who provide Main Street businesses with access to capital and advise hardworking Americans how to create and preserve wealth. The ASA's mission is to promote trust and confidence among investors, facilitate capital formation, and support efficient and competitively balanced capital markets. This advances financial independence, stimulates job creation, and increases prosperity. The ASA has a geographically diverse membership base that spans the Heartland, Southwest, Southeast, Atlantic, and Pacific Northwest regions of the United States. [www.americansecurities.org](http://www.americansecurities.org)

<sup>2</sup> Available at: <https://www.mercatus.org/publication/how-proxy-advisory-services-became-so-powerful>



The ASA recognizes the critical role that proxy advisory firms can play in providing shareholders, particularly large institutional asset managers, with research to inform shareholder voting. However, we believe that previous SEC no-action letters and guidance have had an unintended consequence of enlarging the role and influence of certain proxy advisors without any oversight. Further, several recent reports have documented the level to which proxy advisory firm recommendations contain factual errors and are poorly developed. Allowing asset managers – who owe a fiduciary duty to the Main Street shareholders that invest in funds – to solely rely on inaccurate research harms the ability of retail investors to generate the returns necessary to secure their retirement, send a child to college, or build wealth.

In this context, we applaud the SEC’s recent decision to rescind two 2004 no-action letters which we believe was the primary reason behind overreliance on proxy advisors.<sup>3</sup> These letters effectively allowed institutional investors to outsource their fiduciary voting duty to proxy advisory firms, thus allowing ISS and Glass-Lewis to become the *de facto* standard setters for corporate governance in the United States. The letter also enabled institutional investors to rely on the general policies and procedures a proxy advisory firm may have to manage its own conflicts. This created a situation whereby a proxy advisor vote recommendation on a proposal impacting a particular issuer could be tainted by a significant conflict between the issuer and the proxy advisor (i.e. instances where the issuer is also a consulting client of ISS). Investors, who are unaware of or ignore this conflict, use the vote recommendation to fulfill their fiduciary duty. This harms investors as the conflict may be motivated by considerations other than maximizing shareholder wealth (i.e. political considerations about conflict minerals, climate change, guns, etc.)

Past actions by the SEC have also raised the question as to whether institutional investors are required to vote on *every* proxy. In recent remarks Commissioner Roisman noted that the confusion about whether a requirement exists may be due to a lack of clarity in Staff Legal Bulletin (SLB) 20<sup>4</sup>, which addresses the issue:

*“There appears to be some understandable confusion about what our rules require with respect to whether an adviser must vote. SLB 20 included Question 2, which asks ‘Is an investment advisor required to vote every proxy?’ I can’t help but notice that the 342-word answer did not contain either the word ‘yes’ or ‘no’. I believe the answer should be, in some cases NO.”<sup>5</sup>*

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<sup>3</sup> Available at: <https://www.sec.gov/news/public-statement/statement-regarding-staff-proxy-advisory-letters>

<sup>4</sup> Available at: <https://www.sec.gov/interps/legal/cfslb20.htm>

<sup>5</sup> Available at: [https://www.sec.gov/news/speech/speech-roisman-031819#\\_ftn30](https://www.sec.gov/news/speech/speech-roisman-031819#_ftn30)



The ASA strongly agrees with Commissioner Roisman that there should be instances where investment advisers do not vote their proxies. We believe that the SEC should take additional action to clarify that investment advisers are not required to vote all proxies, particularly when a shareholder proposal deals with an issue not clearly related to maximizing shareholder value.

Certain investment adviser members of the ASA would benefit greatly from this revision, as they must carefully prioritize how to expend resources to best serve their clients. In addition, this clarification will allow them to abstain from voting in appropriate situations, without fear of legal ramifications.

We also support changes to the current proxy advisory system that would subject voting reports produced by proxy advisory firms to the anti-fraud provisions of the proxy solicitation rules.<sup>6</sup> Entities involved in the proxy process – brokers, banks, transfer agents, asset managers, public companies – are all subject to some type of oversight and regulation. Given the influential role played by proxy advisory firms, they should also be subject to minimum standards that the proxy solicitation rules would afford.

Glass Lewis provided an example of the problems inherent in the current system when it threatened to issue recommendations against a company's director candidates if the company availed itself of a no-action letter to adopt a lower special meeting threshold on certain proposals.<sup>7</sup> Clearly, it is counter-intuitive for a company to be punished for availing itself of an official avenue of recourse, particularly by a third-party player which lacks any statutory authority to act as a regulator. We believe that an attempt by one of the largest proxy advisory firms to undermine the role of the SEC as a regulator demonstrates the influence of these firms and their attempts to set broad, general standards for corporate governance.

Finally, the ASA believes that proxy advisors should be prohibited from offering rating and consulting services to issuers on any matter in which they are also being paid by an investor to provide voting recommendations. A new whitepaper released by the Spectrum Group found that 80 percent of retail investors rank conflicts of interest as one of their top three concerns with proxy advisory firms.<sup>8</sup>

More broadly, the Spectrum report found that 85% of survey respondents supported increasing SEC oversight of the proxy advisory industry. These results clearly indicate that retail investors

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<sup>6</sup> Rule 14a-2(b)

<sup>7</sup> Available at: [http://www.glasslewis.com/wp-content/uploads/2018/10/2019\\_GUIDELINES\\_UnitedStates.pdf](http://www.glasslewis.com/wp-content/uploads/2018/10/2019_GUIDELINES_UnitedStates.pdf)

<sup>8</sup> Available at: <http://e09ef08898c431bcc4e7-11b950890bc8bd0c93487608b72ae520.r72.cf2.rackcdn.com/Exile%20of%20Main%20Street-%20A%20Spectrum%20Group%20Whitepaper%20Providing%20a%20Voice%20to%20Retail%20Investors%20on%20the%20Proxy%20Advisory%20Industry.pdf>

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are concerned by the influence and performance of proxy firms, as well as the conflicts of interest that currently exist in their business models.

### **Resubmissions Thresholds**

Despite significant changes to the U.S. stock market and multiple proposals to raise the shareholder proposal resubmission thresholds under Rule 14a-8, the current system has not been updated since 1954.<sup>9</sup> The ASA strongly supports updating the existing resubmission thresholds, specifically for those proposals that are rejected by large margins.

Year after year, companies expend valuable time and resource on shareholder proposals, spending approximately \$150,000 per resolution, totaling more than \$2 million per year for large companies facing 15 or more shareholder proposals<sup>10</sup>. In those instances where resolutions have already been rejected by a clear majority, allowing a minority to continue to reintroduce them on a perennial basis does not benefit shareholders.

Since the current shareholder proposal resubmission guidelines exclude so few proposals even an increase in the resubmission thresholds to 6%-15%-30%, which the SEC proposed in 1997, would still allow the vast proposals to be eligible for resubmission. Specifically, a CII report found that 6%-15%-30% thresholds would only exclude 457 proposals out of 3,620 or roughly 12 percent.<sup>11</sup> Accordingly, we urge the Commission to raise the thresholds to, at a minimum, the levels proposed in 1997. Such a change will do little to impede legitimate measures, while still preventing some of the nuisance proposals that are repeatedly rejected.

### **Conclusion**

We thank the SEC for undertaking this important review of the proxy process and urge it to make the changes outlined above. Our members take seriously their responsibility to advise hardworking and retired Americans on how to create wealth, provide Main Street businesses with access to capital and advisory services, raise capital for schools, hospitals, cities and states and enable institutional investors to increase investment returns. Changes to the proxy process will clearly support these efforts.

Continuing to defer decisions on these important issues on a regular basis risks doing major damage to America's public markets and companies, as well as the investors who rely on them. We believe the proposed changes will allow the proxy process to function more efficiently and

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<sup>9</sup> Available at: [https://docs.wixstatic.com/ugd/72d47f\\_092014c240614a1b9454629039d1c649.pdf](https://docs.wixstatic.com/ugd/72d47f_092014c240614a1b9454629039d1c649.pdf)

<sup>10</sup> House Report 115-904: <https://republicans-financialservices.house.gov/uploadedfiles/crpt-115hrpt904.pdf>

<sup>11</sup> Report available at [https://docs.wixstatic.com/ugd/72d47f\\_092014c240614a1b9454629039d1c649.pdf](https://docs.wixstatic.com/ugd/72d47f_092014c240614a1b9454629039d1c649.pdf)



enable public companies to perform their intended function and increase value for their shareholders.

Sincerely,

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