Council of Institutional Investors®
The voice of corporate governance

Via E-Mail

July 11, 2018

Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: File Number S7-06-18

Dear Mr. Secretary:

I am writing in response to the Securities and Exchange Commission's (SEC or Commission) invitation to comment on its semiannual regulatory agenda.[1] We appreciate that the Commission has advanced the agenda item "Disclosure of Hedging by Employees, Officers and Directors" to the "Division of Corporation Finance—Final Rule Stage," as we have advocated completion and implementation of that rule.[2]

We respectfully reiterate our prior requests that the following two individual agenda items currently listed under the "Division of Corporation Finance—Long Term Actions" be promptly advanced to the Final Rule Stage: "Universal Proxy" and "Listing Standards for Recovery of Erroneously Awarded Compensation."[3] In addition, we also respectfully reiterate our request that the Commission add to its agenda for rulemaking actions amendments to Rule 10b5-1 trading plans.[4]

The Council of Institutional Investors ("CII") is a nonprofit, nonpartisan association of public, corporate and union employee benefit funds, other employee benefit plans, state and local entities charged with investing public assets, and foundations and endowments with combined assets under management exceeding $3.5 trillion. Our member funds include major long-term shareowners with a duty to protect the retirement savings of millions of workers and their

[1] Regulatory Flexibility Agenda, Securities Act Release No. 10,470, Exchange Act Release No. 82,869, Investment Adviser Act Release No. 4,869, Investment Company Act Release No. 33,045, 83 Fed. Reg. 27,280 (June 11, 2018), https://www.gpo.gov/fdsys/pkg/FR-2018-06-11/pdf/2018-11245.pdf.
[2] *Id.* at 27,281; *see, e.g.*, Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors, to Brent J. Fields, Secretary, Securities and Exchange Commission 1 (Feb. 12, 2018) [hereinafter Feb Letter], https://www.cii.org/files/issues_and_advocacy/correspondence/2018/February%2012,%202018%20SEC%20Reg%20Flex%20Letter%20(final).pdf.
[3] *See, e.g.*, Feb Letter, *supra* n.2, at 1 ("We respectfully reiterate our prior request that the following . . . individual agenda items currently listed under the 'Division of Corporation Finance—Long Term Actions' be given a higher priority: 'Universal Proxy,' 'Listing Standards for Recovery of Erroneously Awarded Compensation . . . .").
[4] *See, e.g. id.* ("In addition, we also respectfully request that the Commission add to its agenda for rulemaking action amendments to Rule 10b5-1 trading plans.").

families. Our associate members include a range of asset managers with more than $25 trillion in assets under management.[5]

Universal Proxy

For the benefit of both institutional and retail investors, we continue to believe the Commission should make a priority of finalizing a rule on universal proxy.[6]

As you are aware, in October 2016, the SEC issued for public comment a proposal that would require proxy contestants for corporate board seats to provide shareowners with a universal proxy card that includes the names of both management and dissident director nominees.[7] The universal proxy proposal seeks to address a long-standing problem, was highly careful and well-thought-out, and was responsive to two CII detailed rulemaking petitions.[8]

The comment period for the universal proxy proposal ended on January 9, 2017.[9] More than forty comment letters were received in response to the proposal.[10]

A large majority of commentators supported the universal proxy proposal. In addition to CII,[11] the Investment Company Institute,[12] and the CFA Institute,[13] commentators supporting the proposal included the following investors:

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[5] For more information about the Council of Institutional Investors ("CII"), including its board and members, please visit CII's website at http://www.cii.org.

[6] *See, e.g.*, Feb. Letter, *supra* n.2, at 2 ("For the benefit of both institutional and retail investors, we believe the Commission should make a priority of finalizing a rule on universal proxy.").

[7] *See* Press Release, SEC Proposes Amendments to Require Use of Universal Proxy Cards (Oct. 26, 2016), https://www.sec.gov/news/pressrelease/2016-225.html.

[8] *See* Letter from Glenn Davis, Director of Research, Council of Institutional Investors, to Keith F. Higgins, Director, Division of Corporation Finance, U.S. Securities and Exchange Commission (June 12, 2015), https://www.sec.gov/rules/petitions/2015/petn4-686.pdf; Letter from Glenn Davis, Director of Research, Council of Institutional Investors, to Ms. Elizabeth Murphy, Secretary, U.S. Securities and Exchange Commission (Jan. 8, 2014), https://www.sec.gov/rules/petitions/2014/petn4-672.pdf.

[9] Universal Proxy, Exchange Act Release No. 79,164, Investment Company Act Release No. 32,339, 81 Fed. Reg. 79,122 (proposed rule Oct. 2016), https://www.gpo.gov/fdsys/pkg/FR-2016-11-10/pdf/2016-26349.pdf.

[10] U.S. Securities and Exchange Commission, Comments on Proposed Rule: Universal Proxy (last viewed July 6, 2018), https://www.sec.gov/comments/s7-24-16/s72416.htm.

[11] Letter from Ken Bertsch, Executive Director, Council of Institutional Investors, to Brent J. Fields, Secretary, Securities and Exchange Commission 3 (Dec. 28, 2017) ("With minor enhancements, the proposed framework will provide for a constructive universal proxy regime that gives greater effect to existing shareholder rights."), http://www.cii.org/files/issues_and_advocacy/correspondence/2016/12_28_16_comment_letter_SEC_universal_proxy.pdf.

[12] Letter from Dorothy M. Donohue, Deputy General Counsel, Investment Company Institute 9 (Dec. 19, 2016) ("In general, the adoption of a mandatory universal proxy for operating companies would serve the public interest in giving all shareholders the same voting options, whether they vote by proxy or in person."), https://www.sec.gov/comments/s7-24-16/s72416-1431117-129844.pdf.

[13] Letter from James Allen, CFA, Head, Capital Markets Policy, CFA Institute et al. 1 (Jan. 9, 2017) ("We commend the SEC for addressing this shortcoming of the board voting process by introducing a new Universal Proxy ballot rule that will allow shareowners to effectively split their voting ticket if they chose to do so – without having to attend a company's annual meeting in person."), https://www.sec.gov/comments/s7-24-16/s72416-1473944-130452.pdf.

- Almitas Capital[14]
- California Public Employees' Retirement System (CalSTRS)[15]
- California State Teachers' Retirement System[16]
- Colorado Public Employees' Retirement Association[17]
- Fidelity Investments[18]
- Florida State Board of Administration[19]
- Hermes Equity Ownership Services Limited[20]
- Ohio Public Employees Retirement System[21]
- Comptroller, State of New York[22]
- Trian Fund Management,[23] and the

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[14] Letter from Ron Mass, Managing Director, Almitas Capital 1 (Feb. 3, 2017) ("I support the Commission's proposal to require the use of universal proxies for all contested elections of directors . . . ."), https://www.sec.gov/comments/s7-24-16/s72416-1574799-131790.pdf.

[15] Letter from Marcie Frost, Chief Executive Officer, CalPERS 2 (Jan. 9, 2017) ("We support the proposed amendments which would require proxy contestants to furnish shareowners a universal proxy card; one that includes the names of both management and dissident director nominees in an election contest in a manner that reflects, as closely as possible, the voting process available in-person."), https://www.sec.gov/comments/s7-24-16/s72416-1470820-130402.pdf.

[16] Letter from Anne Sheehan, Director of Corporate Governance, California State Teacher's Retirement System 1 (Jan. 9, 2017) ("We thank the Commission for the opportunity to support and comment on the well-researched, prudent and attentive proposed rule on Universal Proxy."), https://www.sec.gov/comments/s7-24-16/s72416-1471415-130426.pdf.

[17] Letter from Gregory W. Smith, Executive Director, Colorado PERA 2 (Jan. 9, 2017) ("The universal proxy cards for all contested elections would guarantee that shareholders are able to choose from among all board nominees, regardless of whether they voted in person or by proxy."), https://www.sec.gov/comments/s7-24-16/s72416-1471329-130425.pdf.

[18] Letter from Marc R. Bryant, Senior Vice President, Deputy General Counsel, Fidelity Investments 2 (Jan. 9, 2017) ("Fidelity support universal proxy as a logical way to fully accommodate shareholder voting preferences."), https://www.sec.gov/comments/s7-24-16/s72416-1471250-130420.pdf.

[19] Letter from Michael P. McCauley, Senior Officer Investment Programs and Governance, Florida State Board of Administration (SBA) 1 (Jan. 11, 2017) ("SBA staff strongly supports the Commission's effort to provide shareowners with equivalent voting opportunities, whether they vote in person or by proxy."), https://www.sec.gov/comments/s7-24-16/s72416-1481390-130533.pdf.

[20] Letter from Tim Goodman, Director, Hermes Equity Ownership Services Limited 1 (Dec. 23, 2016) ("Our experience is that we would often, possibly usually, prefer to recommend votes for candidates from both the board's and the dissident's slates. This opportunity is currently denied in practice to our clients."), https://www.sec.gov/comments/s7-24-16/s72416-1440887-129987.pdf.

[21] Letter from Karen Carraher, Executive Director, Ohio Public Employees Retirement System et al. 3 (Jan. 4, 2017) ("OPERS believes that the Universal Proxy Requirement should be mandated as proposed, since it more effectively replicates in-person attendance at a shareowners' meeting, which permits shareowners to vote for their preferred combination of nominees from both slates"), https://www.sec.gov/comments/s7-24-16/s72416-1471224-130416.pdf.

[22] Letter from Thomas P. DiNapoli, State Comptroller, State of New York 1 (Jan. 9, 2017) ("I am writing as Trustee of the New York State Common Retirement Fund . . . and administrative head of the New York State and Local Retirement System . . . to express support for the proposed amendments to the federal proxy rules published by the Securities and Exchange Commission . . . in its Release No. 34-79164 pertaining to universal proxies . . . ."), https://www.sec.gov/comments/s7-24-16/s72416-1470796-130406.pdf.

[23] Letter from Brian L. Schorr, Chief Legal Officer and Partner, Trian Fund Management LLP 1 (Jan. 9, 2017) ("We are writing in support of the proposed amendments to the Federal proxy rules published by the U.S. Securities and Exchange Commission . . . in the Release . . . providing for the use of universal proxy cards in contested director elections."), https://www.sec.gov/comments/s7-24-16/s72416-1471095-130411.pdf.

- Washington State Investment Board.[24]

The universal proxy proposal is important for good corporate governance because it removes a long-standing flaw in the U.S. proxy system. That flaw effectively disenfranchises shareowners who vote by proxy cards—the vast majority of shareowners—instead of voting in person.

Currently, shareowners have no practical ability through proxy voting to "split their ticket" and vote for the combination of shareowner and management nominees that they believe best serve their economic interests.[25] As explained by a former SEC Director of Corporation Finance:

> What I haven't heard is a good answer to this simple question: *Why shouldn't a shareholder who votes by proxy have the same voting options as a shareholder who votes in person? Unless someone comes up with a good answer to that question, I think the Commission should move forward with the proposal. . . .*[26]

In addition, Kai Liekefett, of the law firm Sidley Austin, confirms that in several recent proxy fights, including the high profile contests at Automatic Data Processing in 2017 and DuPont in 2015, several large institutional investors were interested in voting for both activist and management candidates, but were not able to do so under the current system.[27]

The universal proxy proposal is consistent with CII's corporate governance best practices for director elections, which states:

> To facilitate the shareholder voting franchise, the opposing sides engaged in a contested election should utilize a proxy card naming all management-nominees and all shareholder-proponent nominees, providing every nominee equal prominence on the proxy card.[28]

While proxy contests are rare events, the right of shareowners to elect directors is a fundamental right of share ownership.[29] Contested elections are pivotal events for companies and for

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[24] Letter from Theresa Whitmarsh, Executive Director, Washington State Investment Board 1 (Jan. 5, 2017) ("The WSIB strongly supports the U.S. Securities and Exchange Commission's proposed release regarding the use of universal proxy cards in contested elections of directors."), https://www.sec.gov/comments/s7-24-16/s72416-1463856-130298.pdf.

[25] Recommendations of the Investor Advisory Committee Regarding SEC Rulemaking to Explore Universal Proxy Ballots 2-4 (adopted July 25, 2013), https://www.sec.gov/spotlight/investor-advisory-committee-2012/universal-proxy-recommendation-072613.pdf.

[26] Keith F. Higgins, Keynote Address at the Practicing Law Institute, Corporate Governance – A Master Class 2 (Mar. 9, 2017) (emphasis added) (on file with CII).

[27] Liana B. Baker & Michelle Price, U.S. Regulator Shelves Reform on Voting in Board Fights-Sources, Reuter News, July 11, 2018, https://www.reuters.com/article/us-sec-universalproxy/u-s-regulator-shelves-reform-on-voting-in-board-fights-sources-idUSKBN1K10FX.

[28] CII, Corporate Governance Policies § 2.2 Director Elections (updated Sept. 15, 2017), http://www.cii.org/files/policies/09_15_17_corp_gov_policies.pdf.

[29] *See, e.g.*, Letter from Jack Ehnes, Chief Executive Officer, CalSTRS, to The Honorable Maxine Waters, Ranking Member, Committee on Financial Services 4 (June 5, 2017) ("Voting for director nominees is a fundamental right, and as a long-term investor, CalSTRS supports the ability to choose among the best suited candidates to represent its interests inside the boardroom."), https://www.calstrs.com/sites/main/files/file-attachments/06-05-2017_maxine_financial_choice_act.pdf.

shareowners, since board seats, and in some cases, board control, are at stake. The dissident group usually advances a specific strategic, operational or financial agenda, so it is important for shareowners to be able to participate fully, regardless of how they vote.

Importantly, requiring a universal proxy would benefit retail investors and institutional investors with relatively smaller positions by allowing them to choose among all board nominees without attending the shareholder meeting, which can involve travel and other costs that may be prohibitive. As Commissioner Stein recently remarked:

> [W]e should adopt final rules regarding the use of universal proxy cards. These rules should recognize that few shareholders can dedicate the time and resources necessary to attend a company's meeting in person and that, in the modern marketplace, most voting is done by proxy.[30]

The current system of competing slates of nominees may be disproportionately confusing to retail investors, who are presented with multiple conflicting proxy cards and may not realize that tabulators count only the most recently submitted card.

In addition, we note that empirical evidence indicates universal proxies do not favor dissidents over management.[31] On this point, a study by Harvard Law School Professor Scott Hirst of proxy contests from 2001 to 2016 found about 15% might have turned out differently with a universal proxy.[32] The study provides empirical evidence that a universal proxy rule would eliminate negative consequences of the current system. The author explains:

> The results . . . show that, of the 15 contexts where universal proxies can be expected to have had distortions between sides, management nominees can be expected to have been favored at 10 contests, and the dissident nominees at five contests. These results are not significantly different from an even split between favoring management and favoring dissident. *This casts doubt on the claim made by opponents of universal proxies that they are likely to help dissidents. If anything. to the extent universal proxies led to different outcomes in contests, they would favor management more frequently than dissidents*.[33]

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[30] Commissioner Kara M. Stein, "Mutualism: Reimaging the Role of Shareholders in Modern Corporate Governance," Speech at Stanford University (Feb. 13, 2018) (footnotes omitted), https://www.sec.gov/news/speech/speech-stein-021318.

[31] *See* Scott Hirst, Harvard Law School, Program on Corporate Governance, Universal Proxies, 35(2) Yale J. On Reg. 437 (2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2805136; *see also* Gail Weinstein, Fried Frank Harris Shriver & Jacobson LLP et al., Expert Analysis, A Practical Assessment of the 'Universal Proxy Card' Plan, Law360, at 4 (Dec. 14, 2016) ("In our view, the universal proxy card mandate, if adopted, would not significantly affect the outcome of . . . activist situations."), http://www.friedfrank.com/siteFiles/Publications/A%20Practical%20Assessment%20Of%20The%20'Universal%20Proxy%20Card'%20Plan.pdf.

[32] Scott Hirst at 437.

[33] *Id*. at 495 (emphasis added).

We note that this proxy season SandRidge Energy, Inc., voluntarily adopted a universal proxy.[34] In doing so they concluded that "[t]he use of a universal proxy card provides shareholders with flexibility and clarity regarding their votes in a contested election and enables shareholders to cast votes for any director nominee . . . without attending the shareholder meeting in person."[35]

Also this proxy season, it was reported that "New Jersey-based Destination Maternity, which had its entire board ousted after losing a shareholder vote in May, would have seen some management nominees keep their seats had investors been able to choose from both slates of candidates, according to people familiar with the vote."[36]

We acknowledge that universal proxies will not resolve all the vote collection and counting issues that were laid bare last year in the contested election of directors at Proctor & Gamble Co.[37] We, however, believe requiring universal proxies would simplify the proxy voting system and lead to voting results that better reflect the intent of retail and institutional shareowners.

Issues Raised at CII Spring Conference

At CII's Spring 2018 conference, SEC Chair Jay Clayton was interviewed by former SEC Chair Elisse Walter.[38] As part of that interview, Chair Walter asked whether there were "any substantive blocks to action that can be addressed by CII and others who favor the proposal."[39]

In his response, Chair Clayton raised two issues that gave him "pause."[40] Those two issues were: (1) the limited solicitation aspect of the proposal, and (2) the circumstance when the election of a dissident results in an incumbent board member refusing to serve.[41] As explained in more detail below, we believe both issues can be easily resolved and are not an impediment to promptly issuing a final rule.[42]

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[34] *See* Press Release, SandRidge Energy, Inc., SandRidge Energy Expands Board of Directors and Adopts Universal Proxy Card (May 7, 2018), https://www.prnewswire.com/news-releases/sandridge-energy-expands-board-of-directors-and-adopts-universal-proxy-card-300643318.html.

[35] *Id.; see, e.g.*, Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors, to Michael L. Bennett, Chairman of the Board of Directors and Chair, Nominating and Governance Committee, SandRidge Energy Inc. 1 (May 10, 2018) (explaining how "the so-called 'bona fide nominee rule'—effectively prevents most issuers and dissident shareholders from availing themselves of the benefits of a universal proxy"), https://www.cii.org/files/issues_and_advocacy/correspondence/2018/May%2010%202018%20Universal%20Proxy%20Letter%20(final)%20(Autosaved).pdf.

[36] Liana B. Baker & Michelle Price.

[37] *See, e.g.*, Alexander Coolidge, How Did P&G Get the Initial Proxy Vote Wrong?, Cincinnati.com, Nov. 16, 2017, https://www.cincinnati.com/story/money/2017/11/16/q-a-nelson-peltz-p-g-and-whats-next-the-snake-pit/870021001/.

[38] *See* CII 2018 Spring Conference, Plenary 1: Interview with the SEC Chair (Mar. 12, 2018), https://www.youtube.com/watch?v=CV7rb-b4sEM.

[39] *See id.*

[40] *See id.*

[41] *See id.*

[42] *See id;* Telephone conversation with Raquel Fox, Senior Advisor to SEC Chairman Jay Clayton (Apr. 25, 2018) (Providing clarification on the two issues raised by Chair Clayton at the CII Spring 2018 conference.).

Issue 1: Limited Solicitation Aspect of Proposal

In raising this issue, Chair Clayton explained:

> That depending on the concentration of holding you could effectively accomplish solicitation by going to much less than a roomful of people, maybe a dinner table full of people. Not sure that that's really where we want to be.[43]

As currently written, the universal proxy proposal "would require dissidents in a contested election subject to Rule 14a-19 to solicit the holders of shares representing at least a majority of the voting power of shares entitled to vote on the election of directors."[44] The Commission explained:

> We believe the threshold we are proposing—a majority of the voting power entitled to vote on the election of directors—strikes an appropriate balance of providing the utility of the mandatory universal proxy system for shareholders while precluding dissidents from capitalizing on the inclusion of dissident nominees on the registrant's universal proxy card without undertaking meaningful solicitation efforts.[45]

The Commission explicitly requested comment on this issue in question # 41 of the proposal.[46] In response to that question, CII's December 2016 comment letter agreed with the SEC's conclusion stating:

> We agree that the proposed requirement "strikes an appropriate balance of providing the utility of the mandatory universal proxy system for shareowners while precluding dissidents from capitalizing on the inclusion of dissident nominees on the registrant's universal proxy card without undertaking meaningful solicitation efforts." We do not believe the dissident should be required to solicit all shareholders to trigger the Universal Proxy Requirement. Many proxy fights are settled early, but among those that go to the active solicitation stage, we believe that in a majority of cases (at least judging from a sample from June 30, 2015, to April 15, 2016), the dissident solicits all shareholders in their first mailing. However, in a significant minority of cases, the dissident solicits less than a majority using a stratified approach that solicits holders above some level of share ownership, because cost of soliciting all shareholders is prohibitive (although often even in these cases the dissident solicits holders of more than 90 percent of shares). CII recognizes that there should be a solicitation requirement to avoid misuse of a universal proxy card. But given the time, effort and cost of preparing and filing a preliminary proxy statement, completing the SEC staff review process, preparing and filing a definitive proxy statement within the prescribed time frame, and solicitation (which will involve significant cost for soliciting any street-name

[43] CII 2018 Spring Conference, Plenary 1: Interview with the SEC Chair.
[44] 81 Fed. Reg. at 79,138.
[45] *Id.*
[46] *Id.*

> holders), a requirement to solicit holders of a majority of shares is sufficient. Moreover, we believe that a universal proxy card sometimes would be tactically useful for companies, and sometimes for dissidents. A decision to set a solicitation requirement at 100% would foster game-playing by a dissident who wishes to avoid a universal proxy, through solicitation just under that level . . . .[47]

Issue 1 solution: Revise proposal to increase solicitation percentage and require a minimum number of shareholders be solicited.

In light of Chair Clayton's view that the proposed minimum solicitation requirement might include "a dinner table full of people" in the case of a registrant with concentrated holdings, we believe one simple resolution to address that issue would be to modify the minimum solicitation requirement in two ways: (1) increase minimum solicitation requirement to 75%; and (2) require that total number of persons solicited is more than 10.

Increase minimum solicitation to 75%

We note that the Commission's own data shows that "requiring dissidents to solicit *all* shareholders would increase the costs borne by dissidents to solicit in a large fraction of typical proxy contests and may prevent some value-enhancing contests from taking place."[48] The data shows that in approximately 97% of proxy contests the dissident solicited shareholders representing more than 50% of the outstanding voting shares.[49]

Despite the Commission's data, we would support a middle ground approach that would revise the universal proxy proposal to require a 75% minimum solicitation requirement. Such an approach would increase the number of shareholders solicited in a significant minority of proxy contents, presumably including some companies with concentrated holdings. In addition, our approach avoids substantially increasing the costs borne by dissidents preventing some value-enhancing contests from taking place.

Require that total number of persons solicited is more than 10

In addition to increasing the proposed minimum solicitation requirement to 75%, we would also support requiring that the total number of persons solicited be more than ten. The "more than 10" requirement is derived from existing Rule 14a-2(b)(2) that provides that the rules generally applicable to dissident proxy solicitations do not apply where the total number of persons solicited is "not more than ten."[50] The proposed revision would also be consistent with the comment letter by CalSTRS that the "SEC consider whether a further amendment to the rule is essential to ensure a minimum number of registered shareholders are solicited . . . ."[51]

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[47] Letter from Ken Bertsch at 21.
[48] *Id*. at 79,176 (emphasis added).
[49] *Id*. at 79,153 ("We estimate that in approximately 97 percent of these proxy contests the dissident solicited shareholders representing more than 50 percent of the outstanding voting shares.").
[50] *See id.* at 79,134 ("the proposed amendments would not apply to solicitations in which the person is not acting on behalf of the registrant and the aggregate number of persons solicited is not more than ten, which are exempt under Rule 14a–2(b)(2)").
[51] Letter from Anne Sheehan at 4.

Notwithstanding Rule 14a-2(b)(2), we would be open to a requirement that the number of persons solicited be greater than 10, for example 25.

Combined, we believe our two modest revisions to the universal proxy proposal would address Chair Clayton's first issue without substantially increasing the costs of a proxy contest.

Issue 2: Circumstance when election of dissident results in incumbent board member refusing to serve

In raising this second issue, Chair Clayton queried "[h]ow do we deal with that that it's more than a one . . . step process on one piece of paper."[52] The universal proxy proposal explicitly requested comment on this issue in question # 5.[53] That question states:

> When adopting the short slate rule, the Commission indicated that the possibility that nominees may not serve if elected with one or more of the opposing party's nominees is best addressed through disclosure. Should we adopt an amendment requiring disclosure about the possibility that nominees may refuse to serve if elected with any of the opposing party's nominees? Should we require disclosure describing how the resulting vacancy can be filled under the registrant's governing documents and applicable state law?[54]

In CII's comment letter we responded to question # 5 as follows:

> We believe it would be beneficial to adopt an amendment requiring disclosure if a party's nominees "will not" serve if elected with any of the opposing party's nominees. Disclosure that they "may not" serve is just a disguised threat, and does not provide the material information that should be disclosed to shareholders. A party's nominees should be required to disclose their actual intentions, not some hedged possibility. Disclosure describing how the resulting vacancy will be filled under the registrant's governing documents and applicable state law should also be required in order to fully equip shareholders with the information required to make an informed decision.[55]

Issue 2 solution: Revise proposal to require disclosure in proxy statement

In light of Chair Clayton's concern about how to deal with the circumstance when election of a dissident results in an incumbent board member refusing to serve, we believe one simple solution, as described in our comment letter, is to require the registrant to disclose in its proxy statement: (1) if a party's nominees will not serve if elected with any of the opposing party's nominees; and (2) how the resulting vacancy will be filled under the registrant's governing documents and applicable state law.

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[52] *See* CII 2018 Spring Conference, Plenary 1: Interview with the SEC Chair.
[53] 81 Fed. Reg. at 79,129.
[54] *Id.*
[55] Letter from Ken Bertsch at 8.

We note that the circumstance raised by Chair Clayton may occur *in any current proxy contest*. We also note that the Commission acknowledges that staff "do not have specific data that suggests the proposed amendments would result in an increase in the reluctance of directors to serve . . . ."[56] Like the SEC, we are unaware of any specific data suggesting that adoption of the universal proxy rule would increase the occurrence of the circumstance Chair Clayton envisions.

We believe our modest proposed revision to the proposal would address Chair Clayton's second issue and do so in a manner that is generally familiar to registrants and dissidents alike because it includes a disclosure consistent with the existing requirements of the SEC's short slate rule.[57] That rule has been in place since 1992.[58]

Majority Voting Disclosure

Finally, the universal proxy proposal provides for a critically important new cost-effective disclosure requirement relating to the *uncontested* election of directors.[59] More specifically, the proposal "expressly requires disclosure in the proxy statement about the treatment and effect of a 'withhold' vote in a director election."[60]

We agree with the Commission that this proposed disclosure, which presumably could be complied with in a single sentence, "would provide shareholders with a better understanding of the effect of their 'withhold' votes on the outcome of the election."[61] Because many shareowners, particularly many retail investors, do not understand that most U.S. public corporations employ a plurality voting standard for the uncontested election of directors,[62] the proposed disclosure is critical.

Under a plurality voting standard in an uncontested election of directors, a "withhold" vote has no legal significance on the outcome of the election.[63] We believe that the proposed disclosure "would make it crystal clear to investors that uncontested plurality elections guarantee victory for all nominees."[64]

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[56] 81 Fed. Reg. at 79,165.
[57] *Id.* at 79,129 ("As the Commission indicated when adopting the short slate rule, a proxy statement should disclose if any nominee has determined to serve only if its nominating party's slate is elected or to resign if one or more of the opposing party's nominees were elected to the board of directors.").
[58] *Id.* at 79,123 n.17.
[59] *Id.* at 79,144.
[60] *Id.*
[61] *Id.*
[62] *See* Council of Institutional Investors, FAQ: Majority Voting for Directors 1 (Jan. 4. 2017) ("Although nearly 90 percent of S&P 500 companies use majority voting in some form, just 29 percent of Russell 2000 companies use a majority vote standard in uncontested elections, according to FactSet."), http://www.cii.org/files/issues_and_advocacy/board_accountability/majority_voting_directors/CII%20Majority%20Voting%20FAQ%201-4-17.pdf; *see also* Jeff Green & Alicia Ritcey, With 'Zombie Directors,' It's the Board of the Living Dead, Bloomberg, Aug. 10, 2017, at 2 (under a plurality voting standard in the election of directors, "since board members often run unopposed, just one positive vote could be enough"), https://www.bloomberg.com/news/articles/2017-08-10/with-zombie-directors-it-s-the-board-of-the-living-dead.
[63] FAQ: Majority Voting for Directors at 1 ("Withholding a vote allows shareholders to communicate their dissatisfaction with a given nominee, but it has no legal effect on the outcome of the election.").
[64] *Id.* at 5.

Consistent with long-standing membership approved policies,[65] CII continues to actively advocate the adoption by all U.S. public companies of a majority, rather than a plurality, voting standard for the uncontested election of directors.[66] Under a majority voting standard, the "withhold" vote is replaced by an "against" vote, helping make board members more responsive to the people they represent.[67]

We believe the proposed disclosure in the universal proxy proposal, if finalized by the Commission, would encourage more U.S. public companies to voluntarily adopt a majority voting standard. The result would be improved corporate governance and potentially higher long-term shareowner value and greater growth in the U.S. public capital markets.[68]

Listing Standards for Recovery of Erroneously Awarded Compensation

As indicated, we continue to support prompt completed action on the SEC's required response to Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) entitled, "Recovery of Erroneously Awarded Compensation."[69]

We note that Section 954 was responsive to the recommendations of the Investors' Working Group (IWG).[70] In their seminal report on U.S. Financial Regulatory Reform, the IWG concluded:

> Federal clawback provisions on unearned executive pay should be strengthened. Clawback policies discourage executives from taking questionable actions that temporarily lift share prices but ultimately result in financial restatements. Senior executives should be required to return unearned bonus and incentive payments that were awarded as a result of fraudulent activity, incorrectly stated financial results or some other cause. The Sarbanes-Oxley Act of 2002 required boards to go after unearned CEO income, but the Act's language is too narrow. It applies only in cases where misconduct is proven—which occurs rarely because most cases result in settlements where charges are neither admitted nor

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[65] § 2.2 Director Elections ("Directors in uncontested elections should be elected by a majority of the votes cast.").
[66] *See* Council of Institutional Investors, Majority Voting for Directors (last visited July 3, 2018) (describing CII "campaign urging companies to adopt majority voting for directors" in the contested election of directors), http://www.cii.org/majority_voting_directors; *see also* Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors, to Mr. Craig S. Phillips, Counselor to the Secretary, U.S. Department of Treasury 9-12 (Aug. 23, 2017) (describing CII's continuing advocacy efforts in support of a listing standard requiring majority voting in the uncontested election of directors"), http://www.cii.org/files/August%2023%202017%20Letter%20to%20Treasury%20v3.pdf.
[67] *See, e.g.*, FAQ: Majority Voting for Directors at 1-2.
[68] *See* Interim Report of the Committee on Capital Markets Regulation 93 (Nov. 30, 2006) ("Even ignoring the entry and exit decisions of firms, public capital markets will be smaller as a result of inadequate shareholder rights [including lack of majority voting], given the reduced valuations resulting from higher agency costs."), http://www.capmktsreg.org/wp-content/uploads/2014/08/Committees-November-2006-Interim-Report.pdf.
[69] Dodd-Frank Wall Street Reform and Consumer Protection Act, H.R. 4173, 111th Cong. § 954 (2010), https://www.gpo.gov/fdsys/pkg/PLAW-111publ203/html/PLAW-111publ203.htm.
[70] S. Rep. No. 111-176, at 136 (Apr. 30, 2010) ("The Investor's Working Group wrote 'federal clawback provisions on unearned executive pay should be strengthened.'"), https://www.congress.gov/111/crpt/srpt176/CRPT-111srpt176.pdf.

> denied—and only covers CEO and CFO compensation. Many courts, moreover, have refused to allow this provision to be enforced via private rights of action.[71]

The SEC's proposed rule to implement Section 954 is generally consistent with CII's membership approved corporate governance policies.[72] Those policies state:

> The compensation committee should ensure that sufficient and appropriate mechanisms and policies (for example, bonus banks and clawback policies) are in place to recover erroneous bonus and incentive awards paid in cash, stock or any other form of remuneration to current or former executive officers, and to prevent such awards from being paid out in the first instance. Awards can be erroneous due to acts or omissions resulting in fraud, financial results that require restatement or some other cause that the committee believes warrants withholding or recovering incentive pay. Incentive-based compensation should be subject to recovery for a period of time of at least three years following discovery of the fraud or cause forming the basis for the recovery. The mechanisms and policies should be publicly disclosed.[73]

Consistent with our policies, we believe the final SEC rule should, as proposed,[74] apply broadly to the compensation of all current or former executive officers whether or not they had control or authority over the company's financial reporting.[75] As we explained in our comment letter to the SEC:

> In our view, establishment of a broad clawback arrangement is an essential element of a meaningful pay for performance philosophy. If executive officers are to be rewarded for "hitting their numbers"—and it turns out they failed to do so—the unearned compensation should generally be recovered notwithstanding the cause of the revision.[76]

We agree with legal experts that broad clawback arrangements may "keep executive officers focused on sound accounting company-wide."[77] Requiring a broad clawback policy appears to be

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[71] Report of the Investors' Working Group, U.S. Financial Regulatory Reform: The Investors' Perspective 23 (July 2009), http://www.cii.org/files/issues_and_advocacy/dodd-frank_act/07_01_09_iwg_report.pdf.

[72] Listing Standards for Recovery of Erroneously Awarded Compensation, Securities Act Release No. 9,861, Exchange Act Release No. 75,342, Investment Company Act Release No. 31,702, 80 Fed. Reg. 41,144 (proposed rule July 2015), https://www.federalregister.gov/articles/2015/07/14/2015-16613/listing-standards-for-recovery-of-erroneously-awarded-compensation.

[73] § 5.5 Pay for Performance.

[74] *See* 80 Fed. Reg. at 41,153 ("the compensation recovery provisions of Section 10D apply without regard to an executive officer's responsibility for preparing the issuer's financial statements").

[75] *See* Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors, to Brent J. Fields, Secretary, U.S. Securities and Exchange Commission 5 (Aug. 27, 2015), http://www.cii.org/files/issues_and_advocacy/correspondence/2015/08_27_15_letter_to_SEC_clawbacks.pdf.

[76] *Id.* (footnotes omitted).

[77] *See, e.g.*, Financial CHOICE Act of 2017, Hearing Before the H. Comm. on Fin. Servs., 115th Cong. 15 (Apr. 26, 2017) (Testimony of Michael S. Barr, The Roy F. and Jean Humphrey Proffitt Professor of Law, University of Michigan Law School), https://financialservices.house.gov/uploadedfiles/hhrg-115-ba00-wstate-mbarr-20170426.pdf.

consistent with the "Commonsense Principles of Corporate Governance" endorsed in 2016 by a number of prominent leaders of U.S. public companies, including Mary Barra, General Motors Company; Jamie Dimon, JPMorgan Chase; Jeff Immelt, GE; and Lowell McAdam, Verizon.[78] Those principles state that "companies should maintain clawback policies for both cash and equity compensation" of management.[79]

We believe the Commission should take note that recent empirical studies have indicated that the adoption of clawback provisions is generally associated with improved financial reporting quality, enhanced investor and auditor confidence in the quality of financial reporting, and reduced audit fees.[80] Moreover, the most recent empirical study we are aware of found that companies with clawbacks generally seek to protect accounting integrity while maintaining and even enhancing the advantages of performance based CFO pay.[81]

We acknowledge Chair Clayton's observation that "several companies . . . have [clawback] policies that go beyond what would be required under Dodd-Frank."[82] However, we believe that empirical evidence suggests a multitude of potential benefits from implementing a rule, as mandated under Dodd-Frank, that applies to all listed companies.

Rule 10b5-1 Trading Plans

Finally, for the benefit of both institutional and retail investors, we continue to believe the Commission should make a priority of proposing amendments to improve Rule 10b5-1 trading plans.[83] We wrote letters on January 18, 2018, to Chair Clayton,[84] May 9, 2013, to Chair Mary

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[78] Commonsense Corporate Governance Principles VII(g) (July 2016), http://www.governanceprinciples.org/.
[79] *Id.*
[80] *See* Gregory L. Prescott & Carol E. Vann, Implications of Clawback Adoption in Executive Compensation Contracts: A Survey of Recent Research, 29 J. Corp. Acct. & Fin. 59, 67 (Jan. 2018) (providing a summary of recent research in the field), https://onlinelibrary.wiley.com/doi/full/10.1002/jcaf.22312.
[81] *See* Peter Kroos et al., Voluntary Clawback Adoption and the Use of Financial Measures in CFO Bonus Plans, 93 Acct. Rev. 213-235 (May/June 2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2312762; *see also* Ben Hiamowitz, Adoption of Clawbacks Means Stronger Link Between Firm Performance and CFO Pay, CPA PracticeAdvisor, June 7, 2018, http://www.cpapracticeadvisor.com/news/12416039/adoption-of-clawbacks-means-stronger-link-between-firm-performance-and-cfo-pay.
[82] Chairman Jay Clayton, Testimony on "Oversight of the U.S. Securities and Exchange Commission," Before the Comm. on Fin, Servs., U.S. H.R. 8-9 & n.50 (June 21, 2018), https://www.sec.gov/news/testimony/testimony-oversight-us-securities-and-exchange-commission; *see* Kathryn Neel, Semler Brossy Consulting Group, LLC, Harv. L. Sch. Forum on Corp. Governance & Fin. Regulation (May 6, 2018) (listing Cognizant Technology Solutions, Wells Fargo, Zions Bancorp, and EBay as companies that have adopted "detrimental conduct" clawback policies); Francine McKenna, Senators Press SEC Chairman on Dodd-Frank Clawbacks, But Equifax Execs Ineligible 5 (Sept. 26, 2017) ("In Wells Fargo's case, . . . [a] stricter policy . . . allowed it to justify a clawback based on reputational damage to the bank and poor risk management"), https://www.marketwatch.com/story/senators-press-sec-chairman-on-dodd-frank-clawbacks-but-equifax-execs-ineligible-2017-09-26; *see also* Michael S. Melbinger, Update on Clawback Policy Issues, Executive Compensation Blog, Winston & Strawn (Oct. 19, 2017) (recommending that "directors should protect themselves and their companies by adopting a strong policy"), https://www.winston.com/en/executive-compensation-blog/update-on-clawback-policy-issues.html.
[83] *See, e.g.*, Feb. Letter, *supra* n.2, at 10 ("Finally, for the benefit of both institutional and retail investors, we believe the Commission should make a priority of proposing amendments to improve Rule 10b5-1 trading plans.").
[84] Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors, to The Honorable Jay Clayton, Chairman, U.S. Securities and Exchange Commission 1 (Jan. 18, 2018),

Jo White,[85] and December 28, 2012, to Chair Elisse Walter[86] regarding our concerns about these plans. Those letters respectfully requested that the Commission should consider potentially pursuing amendments to Rule 10b5-1 that would *require* Rule 10b5-1 plans to adopt the following protocols and guidelines:

- Companies and company insiders should only be permitted to adopt Rule 10b5-1 trading plans when they are permitted to buy or sell securities during company-adopted trading windows, which typically open after the announcement of the financial results from a recently completed fiscal quarter and close prior to the close of the next fiscal quarter;
- Companies and company insiders should be prohibited from adopting multiple, overlapping Rule 10b5-1 plans;
- Rule 10b5-1 plans should be subject to mandatory delay, preferably of three months or more, between the adoption of a Rule 10b5-1 plan and the execution of the first trade pursuant to such a plan;
- Companies and company insiders should not be allowed to make frequent modifications or cancellations of Rule 10b5-1 plans;
- Companies and company insiders should disclose Rule 10b5-1 program adoptions, amendments, terminations and transactions; and
- Boards of companies that have adopted Rule 10b5-1 plans should (1) adopt policies covering plan practices, (2) periodically monitor plan transactions and (3) ensure that company policies discuss plan use in the context of guidelines or requirements on equity hedging, holding and ownership.[87]

If the above protocols had been in place, the widely reported $39 million sale of Intel stock by CEO Brian Krzanich on November 29, 2017, within 30 days of revising his trading plan for the second time during the year, would have been a clear violation of Rule 10b5-1.[88] We are confident that most retail investors would agree with us that Mr. Krzanich's stock sale, just weeks prior to the public announcement of a design flaw in Intel chips, was unfair to other market participants.

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http://www.cii.org/files/issues_and_advocacy/correspondence/2018/January%2018%202018%20Rule%2010b5-1%20(finalI).pdf.

[85] Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors, to The Honorable Mary Jo White, Chairman, U.S. Securities and Exchange Commission 1-2 (May 9, 2013), http://www.cii.org/files/issues_and_advocacy/correspondence/2013/05_09_13_cii_letter_to_sec_rule_10b5-1_trading_plans.pdf.

[86] Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors, to The Honorable Elisse B. Walter, Chairman, U.S. Securities and Exchange Commission 3 (Dec. 28, 2012), http://www.cii.org/files/issues_and_advocacy/correspondence/2012/12_28_12_cii_letter_to_sec_rule%20_10b5-1_trading_plans.pdf.

[87] Letter to The Honorable Mary Jo White at 1; *see* § 5.15b Stock Sales ("10b5-1 program adoptions, amendments, terminations and transactions should be disclosed immediately, and boards of companies using 10b5-1 plans should: (1) adopt policies covering plan practices, (2) periodically monitor plan transactions and (3) ensure that company policies discuss plan use in the context of guidelines or requirements on equity hedging, holding and ownership.").

[88] *See, e.g.*, Stephen Gandel, SEC Needs to Quit Taking Executives' Word on Stock Sales; Gadfly, Wash. Post, Jan. 9, 2017, https://www.washingtonpost.com/business/sec-needs-to-quit-taking-executives-word-on-stock-sales-gadfly/2018/01/09/92cfc61a-f542-11e7-9af7-a50bc3300042_story.html?utm_term=.9e9842673c11.

Unfortunately, Mr. Krzanich's sale was not an unusual occurrence. There is a large body of empirical evidence indicating that Rule 10b5-1 plans have been regularly abused in various ways to facilitate trades based on inside information.[89]

We acknowledge and appreciate that the Commission's recent guidance on public company cybersecurity disclosures includes a discussion of insider trading.[90] That guidance, however, continues to permit "directors, officers, and corporate insiders" to rely on the protections of a flawed rule.[91]

The Commission should promptly propose amendments to Rule 10b5-1 along the lines we have suggested to stop this long-running abuse of the spirit of the rule.

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Thank you for consideration of our views. If we can answer any questions or provide additional information on the Commission's regulatory agenda, please do not hesitate to contact me at [redacted] or [redacted].

Sincerely,

Jeff Mahoney

Jeffrey P. Mahoney
General Counsel

[89] *See* John Shon & Stanley Veliotis, Insiders' Sales Under Rule 10b5-1 Plans and Meeting or Beating Earnings Expectations, 59(9) Mgmt. Sci. iv (Sept. 2013), https://pubsonline.informs.org/doi/abs/10.1287/mnsc.1120.1669?journalCode=mnsc; *see also* Susan Pulliam & Rob Barry, Executives' Good Luck in Trading Own Stock, Wall. St. J., Nov. 27, 2012, https://www.wsj.com/articles/SB10000872396390444100404577641463717344178.

[90] Commission Statement and Guidance on Public Company Cybersecurity Disclosures, Securities Act Release No. 10,459, Exchange Act Release No. 82,746, 83 Fed. Reg. 8,166, 8,171-72 (interpretation Feb. 26, 2018) ("information about a company's cybersecurity risks and incidents may be material nonpublic information, and directors, officers, and other corporate insiders would violate the antifraud provisions if they trade the company's securities in breach of their duty of trust or confidence while in possession of that material nonpublic information"), https://www.gpo.gov/fdsys/pkg/FR-2018-02-26/pdf/2018-03858.pdf.

[91] *See* 83 Fed. Reg. at 8,171 n.60 ("[t]his would not preclude directors, officers, and other corporate insiders from relying on Exchange Act Rule 10b5–1 if all conditions of that rule are met").