



February 3, 2020

Ms. Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-0609

Re: File No. S7-22-19: Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice

Dear Ms. Countryman,

The Biotechnology Innovation Organization (BIO) appreciates the opportunity to provide comments to the Securities and Exchange Commission (SEC) on File No. S7-22-19, its proposal to amend the exemptions from the proxy rules for proxy voting advice.

BIO represents nearly 1,000 biotech companies, academic institutions, state biotechnology centers, and related organizations in all 50 states. BIO member companies – the vast majority of which are pre-revenue – 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. These emerging biotech companies are unique compared to other industries in that they operate, on average, for 10 to 15 years before generating product revenue and remain unprofitable during this period as resources are largely poured into R&D.

BIO believes that proxy voting advice businesses should be more transparent and open to input in their standard-setting processes, particularly with regard to issues unique to small businesses. BIO therefore strongly supports the proposed amendments, which would increase transparency by requiring proxy voting advice businesses to comply with certain requirements for disclosing conflicts of interest, allowing companies the right to review and respond to recommendations, and requiring proxy firms to include the company's response in the firms' materials provided to clients.

I. Proxy Advisory Firms and the Biotechnology Industry

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, 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. Accordingly, we have long held concerns about the oversized role of proxy voting advice businesses and their impact on our investors.

Despite their significant influence on emerging companies, proxy voting advice businesses (the universe of which is functionally limited to just two firms) generally refuse to engage in

a productive or transparent dialogue with smaller issuers, instead relying on one-size-fits-all recommendations that do not take into account a company's or its shareholders' unique circumstances. These one-size-fits-all recommendations, developed with minimal input from the company, do not accurately reflect the true nature of an emerging biotech, and are often focused on quarterly metrics rather than long-term scientific advancement and shareholder value creation.

Proxy voting advice businesses have developed 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 on a management proposal can result in a 13.6% to 20.6% sway in the vote.¹ The two largest firms wield such power in the proxy process that emerging biotech companies see a substantial decrease in shareholder support if a proxy voting advice business is in opposition to the proposal.

As noted in the proposing release, there have been some efforts by the largest proxy voting advice businesses to share certain information with registrants. Unfortunately, these efforts have been restrictive and limited. In one case, the opportunity to review is available only to Standard and Poor's 500 Index companies. Companies not on the S&P 500 are precluded from receiving and reviewing the information. In another case, the opportunity is only available to registrants who are willing to pay the proxy voting advice business to obtain access. For biotech companies, where every dollar diverted from the lab may potentially delay the availability of their treatments to patients, this is an unreasonable financial burden. Despite these limited efforts, the fact remains that the proxy voting advice businesses are not held accountable for the accuracy, reliability or transparency of their recommendations.

Proxy voting advice businesses utilize specific methodologies to formulate voting recommendations, but companies and investors have no visibility into those secret formulas (unless, in some circumstances, they pay fees to obtain them). Without basic standards for transparency, companies are left in the dark with no ability to predict how the proxy voting advice businesses will approach a proxy proposal.

Biotech companies have unique business models that are often disregarded by proxy voting advice businesses. Instead, the proxy voting advice businesses 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 voting advice businesses, 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.

¹ http://www.shareholderforum.com/access/Library/20130510_Larcker-McCall-Ormazabal.pdf

Given the impact that proxy voting advice businesses have on emerging biotech companies, BIO strongly supports the SEC's proposed rule to bring firms that furnish proxy voting advice under the scope of Section 14(a) of the Exchange Act. Clarifying that proxy voting advice generally constitutes a solicitation is a welcome step that enables the SEC to make the reforms it has proposed to address proxy voting advice businesses' conflicts of interest, lack of engagement with registrants, and misleading statements.

II. Conflicts of Interest

As the SEC observes, "[p]roxy voting advice businesses engage in activities or have relationships that could affect the objectivity or reliability of their advice, which may need to be disclosed in order for their clients to assess the impact and materiality of any actual or potential conflicts of interest with respect to a voting recommendation."

BIO has long expressed concerns about the conflicts of interest inherent in the business model or ownership structure of the predominant two proxy voting advice businesses. In one case, the related consulting service charges public companies a fee to learn how to best comply with its voting policies and obtain favorable recommendations in the future. This problematic conflict of interest is even recognized by Glass Lewis, which stated in a 2018 letter, "We believe the provision of consulting services creates a problematic conflict of interest that goes against the very governance principles that proxy advisors like ourselves advocate...Further, a consulting business is not only in conflict with the interests of our clients, but in conflict with the interests of the companies who are entitled to a fair, reasonable and independent assessment."² In the other, the 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 voting advice businesses are anything but independent.

BIO applauds the SEC for proposing to implement enhanced conflicts of interest disclosures to address conflicts of interest such as those examples provided in the proposing release and those experienced by BIO members. Under the SEC's proposal, proxy firms would need to prominently disclose in the proxy voting advice detailed information regarding any material interests (direct or indirect) in the matter or parties concerning which it is providing advice; any transaction or relationship between the proxy firm (or its affiliates) and the registrant; any other information regarding the interest, transaction, or relationship of the proxy firm that is material to assessing the objectivity of the advice, and any policies and procedures used to identify, and steps taken to address, any such conflicts. BIO appreciates that the proposal makes clear that conflicts disclosures must be sufficiently prominent and detailed, and non-boilerplate, in order to ensure investors can understand the risks that the conflicts pose.

BIO supports these proposed enhanced conflict of interest disclosures as an important step in addressing this significant issue. To increase the likelihood that the disclosure is seen and considered by clients, BIO submits that the conflicts should be disclosed in the proxy voting advice, rather than provided separately. For the same reason, to the extent the proxy voting advice business uses an electronic medium to convey its voting advice, the disclosure should be conveyed in the same manner. Additionally, BIO would support targeted limitations on a proxy voting advice business's ability to automatically vote their clients'

² Glass Lewis Letter to Senator Dean Heller, available at https://www.glasslewis.com/wp-content/uploads/2018/06/Glass-Lewis-Response-to-May-9-2018-Chairman-Heller-Letter_0601_FINAL.pdf

shares in certain instances so that the proposed conflicts disclosures are more likely to be reviewed by investors.

In addition, BIO suggests that proxy voting advice businesses also should be required to more effectively mitigate these conflicts and, thus, we would also urge the SEC to consider additional actions to hold the proxy voting advice businesses accountable for mitigation of these conflicts as well. Proxy voting advice businesses have stated in the past that their conflicts of interest are effectively mitigated via a firewall wherein their registrant consulting operations acts independently of their voting advice operations. In our companies' experiences however, irrespective of the controls the proxy voting advice business has, questions have arisen regarding just how robust and effective the firewall truly is. Irrespective of any specific companies' firewalls, BIO strongly believes an industry standard for mitigating conflicts of interest is in the best interests of registrants and shareholders alike. In the proposing release, reasonable alternatives that are discussed include mandating conflicts of interest disclosure be made publicly rather than just to clients. BIO supports this greater disclosure.

III. Ability to Review and Provide Feedback on Proxy Voting Advice by Registrants

The SEC's proposed amendments would provide an opportunity for registrants to review and provide feedback on the proxy voting advice before the proxy voting advice business distributes the voting advice to its clients. The proposal would provide registrants a limited amount of time to review the voting advice and provide feedback.

The amount of time available to the registrant would depend on how far in advance of the shareholder meeting the registrant filed its definitive proxy statement. If the registrant files its definitive proxy statement 45 days or more in advance of the shareholder meeting, the registrant would be entitled to at least five business days to review. If the definitive proxy statement is filed between 25 and 45 days prior to the shareholder meeting, the registrant would be entitled to three business days to review. If statements filed less than 25 days in advance, the registrant would not be entitled to advance review.

BIO strongly supports providing a meaningful opportunity for registrants to review the voting advice and provide feedback. BIO believes that the entirety of the voting advice should be available for review by the registrant, including voting advice included in so-called "specialty" reports. This will eliminate the need for any judgements about which sections to make available for review and ensure that the registrant will be able to review and provide feedback on any aspect it deems necessary. In addition, we urge the SEC to include a requirement that proxy voting advice businesses 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.

Further, BIO notes that in some cases, the process may take time for the registrant to review and formulate its response. For example, the process will likely include both internal and outside SEC counsel review, a process that will be hard to expedite. This is especially true if the voting advice recommends against a director, or what might be deemed a controversial proposal. Accordingly, BIO recommends that companies be allowed a minimum of five business days to review and provide feedback if they file the definitive proxy statement more than 25 days in advance.

BIO also contends that registrant review is unlikely to impact the independence and impartiality of proxy voting advice businesses' reports. The proposing release solicits comment on this topic, but it is clear in the proposal that proxy voting advice businesses



would be free to ignore suggested edits from registrants – so the only changes made to the final reports will be those with which the proxy voting advice business agrees.

IV. Opportunity to Include A Registrant Response within Proxy Voting Advice

In addition to the review and feedback period, the proposal would require proxy voting advice businesses to provide registrants with a final notice of voting advice at least two business days prior to delivery of the voting advice to clients. This requirement would be in effect regardless of whether the registrant initially reviewed and provided feedback on the voting advice. Registrants would have the opportunity to provide a response to the voting advice and request that a hyperlink to the response be included with the voting advice.

BIO supports the requirement to allow all registrants an opportunity to provide a statement in response to the voting advice. We also agree with the SEC that companies should not be required to participate in the five-day review and feedback process to be eligible to submit a registrant response, that all voting advice should be available for registrant response (not just reports with an adverse recommendation), and that proxy voting advice businesses should not be allowed to charge companies a fee to provide feedback or submit a registrant response. We are concerned, however, that the proposed two-day timeframe is not long enough for smaller registrants such as emerging biotechs to review any changes to the voting advice and prepare their response. BIO requests that this time frame be extended to at least 3-5 days prior to the distribution of the voting advice.

Further, BIO has concerns that merely requiring proxy voting advice businesses to provide a hyperlink in its materials to a registrant's statement risks having the statement overlooked or not given sufficient weight in a client's consideration of the voting advice. Accordingly, BIO suggests allowing registrants the option of requesting a hyperlink to the statement or inclusion of the full written statement in the voting advice delivered to clients.

Similarly, in instances where proxy voting advice businesses provide voting execution services, BIO has concerns that automatic submission could mean clients are less likely to consider a registrant's response to the voting statement. Accordingly, BIO supports measures that would increase the likelihood that the registrant's statement is taken into account, such as disabling the auto-submission of votes when a registrant has submitted a response, or disabling auto-submission unless the client accesses the registrant's response or otherwise confirms the pre-populated voting choices.

V. Expanding Prohibitions Against False or Misleading Statements

BIO supports the expanded prohibitions against false or misleading statements that the SEC proposes. Significantly, BIO agrees that it is important for proxy voting advice businesses to clarify when a negative voting recommendation is based on the proxy voting advice business's own determination that a registrant's conduct or disclosure is inadequate, notwithstanding that the conduct or disclosure meets applicable SEC requirements.

For example, a recently issued policy statement by one of the two large proxy voting advice businesses may undermine the SEC's attempt to ease regulatory disclosure burdens on Smaller Reporting Companies (SRCs) to promote capital formation.³ SRCs are only required

³ Glass Lewis 2019 Proxy Paper Guidelines: An Overview of the Glass Lewis Approach to Proxy Advice; available at https://www.glasslewis.com/wp-content/uploads/2018/10/2019_GUIDELINES_UnitedStates.pdf

to disclose two years of summary compensation table information rather than the three years required of larger issuers. However, the proxy voting advice business's policy statement states that that they will consider the impact of the one-year reduction in compensation disclosure in their analysis – irrespective of an issuer's SRC status. If an SRC's executive leadership team thinks that it will get an adverse voting recommendation from the highly influential proxy voting advice businesses, which wield a significant impact on the voting outcome, they would be less inclined to utilize the disclosure exemptions made available to them by the SEC. BIO has been an ardent supporter of the scaled exemptions for smaller public companies.⁴ These scaled disclosure and compliance requirements, which can yield significant cost savings for emerging biotechs, are an important recognition by the SEC that overly burdensome regulations are unnecessary for registrants and shareholders alike. By misrepresenting their opinions to shareholders regarding these exemptions, proxy voting advice businesses put companies at risk of needlessly diverting their capital from science to compliance.

Under the proposal, proxy voting advice businesses would now need to disclose the use of standards or requirements that materially differ from relevant SEC standards or requirements. This disclosure will help avoid the misimpression that the negative voting recommendation is based on a registrant's failure to comply with SEC requirements, when it is actually based on the proxy voting advice business's own distinct criteria. Unless the distinction is clearly delineated, proxy voting advice businesses may ultimately usurp the SEC's important role as the standard setter for small public companies.

VI. Conclusion

BIO applauds the SEC for taking a proactive approach in amending the exemptions from the proxy rules for proxy voting advice. If adopted, the proposal will significantly improve proxy firm transparency without sacrificing investor protections.

BIO looks forward to working with the SEC on this important issue, as well as other matters which benefit the biotech sector entering and staying in the public markets. If we can provide further information regarding these comments, please contact me at [REDACTED].

Sincerely,



Cameron Arterton
Vice President
Biotechnology Innovation Organization (BIO)

⁴ See e.g. BIO Comment on Amendments to Smaller Reporting Company Definition, available at: <https://www.sec.gov/comments/s7-12-16/s71216-14.pdf>; BIO Comment on Amendments to the Accelerated Filer and Large Accelerated Filer Definitions, available at: <https://www.sec.gov/comments/s7-06-19/s70619-5881309-188765.pdf>