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February 3, 2020

Ms. Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7-22-19

Dear Ms. Countryman:

Nasdaq, Inc. (“Nasdaq”)¹ appreciates the opportunity to comment on the Commission’s proposed amendments to the exemptions from the proxy rules for proxy voting advice businesses (the “Proposal”).² The Proposal is the natural evolution of the Commission’s laudable consideration of this issue over the past decade³ and we applaud the Commission for its continued efforts to strengthen the integrity of the proxy voting system. Nasdaq recognizes the utility of proxy voting advice businesses (“proxy advisors”) and agrees with Chairman Clayton that “shareholder engagement is a hallmark of our public capital markets and the proxy process is a fundamental component of that engagement.”⁴ We commend the Commission for its efforts to construct a framework that increases transparency, accuracy and accountability in the proxy voting advice industry “without generating undue costs or delays that might adversely affect the timely provision of proxy voting advice.”⁵

Nasdaq operates regulated entities in the United States, Canada, the Nordics and Baltics including The Nasdaq Stock Market, which is home to over 3,000 listings that drive the global economy and provide investment opportunities for Main Street investors. We are a self-regulatory organization mandated to protect investors and the public interest. Nasdaq is also a listed company and is subject to the same regulations as other public companies, including the proxy rules. Thus, Nasdaq is able to bring a unique perspective to these issues.

Nasdaq receives valuable feedback from our listed companies, companies seeking to access the public markets and their investors about issues that are important to them. We collaborate with the

¹ Nasdaq (Nasdaq: NDAQ) is a global technology company serving the capital markets and other industries. Our diverse offering of data, analytics, software and services enables clients to optimize and execute their business vision with confidence. To learn more about the company, technology solutions and career opportunities, visit us on [LinkedIn](#), on Twitter [@Nasdaq](#), or at www.nasdaq.com.

² *Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice*, Securities Exchange Act Release No. 34-87457 (November 5, 2019), 84 FR 66518 (December 4, 2019).

³ *See* Appendix B, pages 5-7, for an overview of the Commission’s past efforts.

⁴ *See* Statement Announcing SEC Staff Roundtable on the Proxy Process (July 30, 2018), available at: <https://www.sec.gov/news/public-statement/statement-announcing-sec-staff-roundtable-proxy-process>.

⁵ *See* Proposal at 12.

public companies that have chosen to list on Nasdaq in the United States, and communicate with these companies and their investors about the public company model. While these companies may have different perspectives on many issues, one topic regularly raised by them is a concern about the increasing compliance costs and regulatory burdens faced by public companies. We have repeatedly heard that the way proxy advisors operate unnecessarily increases the costs of being a public company, creates disincentives for companies to go public and further distances companies from their shareholders. We believe the Commission's Proposal is an important step forward to increase shareholder engagement and promote further growth and public market participation.

Nasdaq encouraged companies to submit their own letters to the Commission; however, many were reluctant to draw attention to themselves by publicly commenting on the Proposal. In order to obtain feedback from Nasdaq-listed companies about their experiences with proxy advisory firms and their views on the Proposal, Nasdaq conducted telephone calls in January 2020 ("2020 Issuer Outreach"). To maintain confidentiality, we have summarized each company's feedback anonymously in Appendix A.⁶ Nasdaq also partnered with the U.S. Chamber of Commerce Center for Capital Markets Competitiveness in 2019 to conduct its annual survey of public company experiences with proxy advisory firms (the "2019 Chamber Survey"), attached as Appendix B.

Overview of Concerns with the Current System

As the Commission notes, institutional share ownership has grown significantly in recent years, accounting for 70-80% of share ownership of public companies.⁷ Given the number of public companies, the large number of proposals placed on each company's proxy, the limited time to consider these proposals, and historically viewing SEC rules as requiring most institutional investors to vote all items on the proxy, institutional investors have come to rely on proxy advisors. Nasdaq recognizes that proxy advisors provide important research on public companies and can streamline the voting process for institutional investors. Unfortunately, the services that proxy advisors provide to their clients cannot be evaluated in a meaningful manner due to a lack of transparency and inherent conflicts of interest.

The current system is dominated by two firms that together control 97% of the market for proxy advisory services.⁸ Some investors may use reports provided by these firms as one data point among many in an independent process to arrive at a voting decision. However, research suggests that these reports are the determining factor for many investors. A 2018 study conducted by the Manhattan Institute found that "proxy advisors have a material, if unspecified, influence over institutional voting behavior and therefore also voting outcomes. A recommendation to vote against a proposal is associated with a reduction in the favorable vote count by 15%-30%."⁹ In the 2019 Chamber Survey, several companies reported that 15%-40% of their outstanding shares were robo-voted by institutional investors in line with ISS' voting recommendation within two days after its report was issued. "The same

⁶ Nasdaq spoke directly to each of these companies and each summary was reviewed for accuracy by the company. To promote candor on the part of the companies, we promised to anonymize their identity.

⁷ See Proposal at 6.

⁸ U.S. Chamber's Center for Capital Markets Competitiveness and Nasdaq, *2019 Proxy Season Survey* (November 21, 2019), available at: https://www.uschamber.com/sites/default/files/ccmc_proxyseasonsurvey2019_v1.pdf.

⁹ James R. Copland, David F. Larcker and Brian Tayan, *Proxy Advisory Firms: Empirical Evidence and the Case for Reform*, Manhattan Institute (May 2018) at 13, available at: <https://media4.manhattan-institute.org/sites/default/files/R-JC-0518-v2.pdf>.

issue arose with Glass Lewis, although on a smaller scale, with several companies reporting that between 5% and 10% of their shares voted automatically with a Glass Lewis recommendation.”¹⁰

The stories we hear further suggest that proxy advisors exert an outsized influence on public companies. Companies have told us that they feel pressured to shape their corporate governance practices and shareholder proposals to avoid a negative vote recommendation from proxy advisors, which stifles meaningful debate about corporate governance and may not be in the best interest of the company or its shareholders.¹¹ Indeed, 29% of respondents in the 2019 Chamber Survey notified proxy advisors and their clients of recommendations that did not advance the best economic interest of shareholders.¹²

The Proposal is an important step towards increasing transparency, accuracy and accountability in the proxy advisory industry. It is imperative that proxy advisors have complete and accurate information when crafting voting recommendations that impact the sound governance of public companies. It is equally important that institutional investors are aware of any conflicts of interest when using proxy voting reports to make voting decisions that ultimately impact millions of Main Street investors saving for retirement or a child’s education.¹³

Previous U.S. and International Regulatory and Legislative Initiatives

Over the past decade, concerns expressed by three former SEC Commissioners¹⁴ have been shared by Republicans and Democrats in Congress,¹⁵ the U.S. Government Accountability Office,¹⁶

¹⁰ See 2019 Chamber Survey at 12.

¹¹ See Edward S. Knight, *Raising the Curtain on Proxy Advisers*, THE WALL STREET JOURNAL, October 7, 2013, available at: <https://www.wsj.com/articles/raising-the-curtain-on-proxy-advisersraising-the-curtain-on-proxy-advisers-1381179479?ns=prod/accounts-wsj>; see also Letter from Mr. Edward S. Knight, Executive Vice President, General Counsel and Chief Regulatory Officer, Nasdaq, to Ms. Elizabeth M. Murphy, Esq., U.S. Securities and Exchange Commission, dated October 8, 2013, available at: <https://www.sec.gov/rules/petitions/2013/petn4-666.pdf> (“Nasdaq 2013 Petition”).

¹² See 2019 Chamber Survey at 11.

¹³ A 2019 survey of 5,000 retail investors conducted by Spectrem Group found that 81% of respondents support increased oversight of proxy advisors. See Spectrem Group, *Reclaiming Main Street: SEC Hears Retail Investors’ Cries for Proxy Advisory Oversight*, January 10, 2020, at 6, available at: <https://spectrem.com/Content/Whitepaper/reclaiming-main-street-white-paper.aspx> (“2019 Spectrem Group Survey”).

¹⁴ See Statement of The Honorable Harvey L. Pitt, *Examining the Market Power and Impact of Proxy Advisory Firms* (June 5, 2013), available at: <https://www.govinfo.gov/content/pkg/CHRG-113hhrg81762/pdf/CHRG-113hhrg81762.pdf>; see also Commissioner Daniel M. Gallagher, *Remarks before the Society of Corporate Secretaries & Governance Professionals*, 67th National Congress, July 11, 2013, available at: <http://www.sec.gov/News/Speech/Detail/Speech/1370539700301>; see also Commissioner Troy A. Paredes’ remarks before the Society of Corporate Secretaries & Governance Professionals, 66th National Conference on “The Shape of Things to Come” (July 13, 2012), available at: <http://www.sec.gov/News/Speech/Detail/Speech/1365171490796>.

¹⁵ See Appendix B, pages 5-6.

¹⁶ See U.S. Government Accountability Office, “Corporate Shareholder Meetings: Proxy Advisory Firms’ Role in Voting and Corporate Governance Practices” *Report to the Chairman, Subcommittee on Economic Policy, Committee on Banking, Housing, and Urban Affairs, U.S. Senate* (November 2016), available at: <https://www.gao.gov/assets/690/681050.pdf>.

academic researchers,¹⁷ the press,¹⁸ public companies,¹⁹ retail investors²⁰ and Nasdaq.²¹ The Commission took incremental steps in addressing these concerns by issuing Staff Legal Bulletin 20 in 2014, withdrawing two no-action letters in 2018, and issuing guidance on the application of the federal proxy rules to voting advice and investment advisers' proxy voting responsibilities in 2019. But these changes did not sufficiently address concerns with the lack of transparency, accountability and inherent conflicts of interest in the proxy advisory industry.

These concerns are not unique to the United States. International regulators have responded by adopting measures to increase transparency and disclosure of conflicts of interest. The Chairman of the Autorité des Marchés Financiers ("AMF") in France, Robert Ophèle, recognized that "proxy advisors have been criticised for their lack of true dialogue with issuers, a 'mechanical' approach that does not take into account the specific characteristics of French law and the French market, as well as analyses marred by conflicts of interest. This is because some of these proxy advisors sometimes provide consulting services to issuers for whom they also assess resolutions submitted to the general meeting."²² In 2011, the AMF recommended that proxy advisors, among other things, manage any conflicts of interest transparently and provide companies with a draft review process.

In 2014, European Commission proposed amendments to the Shareholders Rights Directive designed to increase the accuracy and reliability of voting recommendations. The European Commission expressed concern that "[t]he different services provided to issuers, such as governance consultancy, may affect the independence of the proxy advisor and their ability to provide an objective and reliable advice. As proxy advisors are subject to conflicts of interests, appropriate procedures for the prevention, detection and treatment of such conflicts are necessary. In view of the important role of the recommendations of proxy advisors these should be accurate and reliable."²³

In June 2019, the amended Shareholders Rights Directive ("SRD II") entered into force. SRD II

¹⁷ See *supra* note 9; see also James K. Glassman and J.W. Verret, *How to Fix Our Broken Advisory System*, Mercatus Center (2013), available at:

http://mercatus.org/sites/default/files/Glassman_ProxyAdvisorySystem_04152013.pdf.

¹⁸ See The Editorial Board, "The Proxy Advisors' Veto," THE WALL STREET JOURNAL, August 10, 2018, available at: <https://www.wsj.com/articles/the-proxy-advisers-veto-1533941976>.

¹⁹ See Letter from Nasdaq et. al., to The Honorable Jay Clayton, Chairman, Securities and Exchange Commission, dated February 4, 2019, available at: <https://www.sec.gov/comments/4-725/4725-4872519-177389.pdf> ("2019 Public Company Letter"); see also Letter from 1st Source Corporation et. al. to Elizabeth M. Murphy, Esq., Secretary, U.S. Securities and Exchange Commission, dated December 4, 2013, available at: <https://www.sec.gov/comments/4-666/4666-4.pdf> ("2013 Public Company Letter").

²⁰ See 2019 Spectrem Group Survey.

²¹ See *supra* note 11; see also Nasdaq, *The Promise of Market Reform: Reigniting America's Economic Engine*, May 2017, available at: <http://business.nasdaq.com/revitalize> ("Revitalize"); see also Letter from John A. Zecca, Senior Vice President, General Counsel, North America and Chief Regulatory Officer, Nasdaq, to Ms. Vanessa Countryman, Secretary, U.S. Securities and Exchange Commission, dated July 18, 2019, available at: <https://www.sec.gov/comments/s7-26-18/s72618-5825362-187511.pdf>.

²² See Speech by Robert Ophèle, AMF Chairman - Droit & Croissance Conference "Corporate governance and shareholders engagement: the new normal conference" (October 22, 2019), available at: https://www.amf-france.org/en_US/Actualites/Prises-de-paroles/Archives/Annee-2016?docId=workspace%3A%2F%2FspacesStore%2F83263e6e-944c-4ed3-9737-74e255d7e8bd&langSwitch=true.

²³ European Commission, *Staff Working Document Impact Assessment* (September 4, 2014) at 4.6, available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=SWD:2014:0127:FIN>.

requires proxy advisors who operate in the EU to publicly disclose on their website, among other things, their code of conduct; details of their methodologies and information sources; whether and how they take into account national market, legal and regulatory and company-specific conditions; the nature and extent of their dialogues with companies, if any; and their policy regarding the prevention and management of potential conflicts of interest. Proxy advisors are also required to identify any actual or potential conflicts of interest or business relationships that may influence the preparation of their voting recommendations and disclose the conflicts to clients, along with the actions the proxy advisor has taken to eliminate, mitigate or manage the conflict.²⁴ In implementing the requirements of SRD II into national law, the U.K. authorized the Financial Conduct Authority to enforce the regulations with financial penalties.²⁵

The experience of international regulators demonstrates that specific standards are necessary to promote transparency, accountability and fairness in an industry dominated globally by two companies. The Proposal would help ensure that proxy voting reports provided to institutional investors in the United States are at least of similar quality and accuracy to those provided to investors in jurisdictions where proxy advisors are subject to prescriptive regulations. ISS states publicly on its website that it believes the review process provided to French companies “helps improving the accuracy and quality of its analyses, an outcome that is in the best interests of both the institutional investors for whom the analyses are prepared, as well as for the issuers that are the subject of these reports.”²⁶ U.S. companies and investors should benefit from similar checks and balances so that the U.S. capital markets remain the envy of the world.

Analysis of the Proposed Rule

Under the Proposal, proxy voting advice would be considered a “solicitation” under the federal proxy rules, but would be exempt from the information and filing requirements thereunder if a proxy advisor: (1) discloses material conflicts of interest; (2) provides the company an opportunity to review and provide feedback on its draft voting advice; and (3) provides the company an opportunity to issue a response to the voting advice and includes a hyperlink to that response in its voting advice. We support the reiteration of the Commission’s longstanding view of the term “solicitation” and the proposed conditions to the exemptions further described below.

Conflicts of Interest

Currently, proxy advisors are required to disclose significant relationships or material interests in order to qualify for an exemption from the federal proxy rules, which has resulted in vague or

²⁴ See Article 3j, *Directive (EU) 2017/828 of the European Parliament and of the Council of 17 May 2017 amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement*, available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32017L0828>; see also European Commission, “Shareholders’ rights directive Q&A” (March 14, 2017), available at: https://ec.europa.eu/commission/presscorner/detail/en/MEMO_17_592.

²⁵ See Regulation 12, *Proxy Advisors (Shareholders’ Rights) Regulations 2019*, available at: <http://www.legislation.gov.uk/uksi/2019/926/made>; see also Explanatory Memorandum to the Proxy Advisors (Shareholders’ Rights) Regulations 2019 (2019 No. 926) available at: http://www.legislation.gov.uk/uksi/2019/926/pdfs/uksiem_20190926_en.pdf.

²⁶ See Institutional Shareholder Services Inc., *French Market Engagement Disclosure* (accessed January 23, 2020), available at: <https://www.issgovernance.com/policy-gateway/french-market-engagement-disclosure/>.

boilerplate disclosure.²⁷ Under the Proposal, a proxy advisor would be required to disclose in its proxy voting advice: (i) any material interests, direct or indirect, of the proxy advisor (or its affiliates) in the matter or parties concerning which it is providing the advice; (ii) any material transaction or relationship with the company, a shareholder proponent or other soliciting person, or affiliates thereof, connected with the matter covered by the proxy voting advice; (iii) any other information regarding the interest, transaction or relationship of the proxy advisor or its affiliates that is material to assessing the objectivity of the proxy voting advice; and (iv) any policies and procedures used to identify, as well as the steps taken to address, any such material conflicts of interest.²⁸

In a 2013 petition supported by 58 public companies, Nasdaq called for the Commission to condition such exemptions on public disclosure of any and all business relationships that may give rise to conflicts of interest.²⁹ Although the Proposal does not go as far as to require public disclosure of all conflicts, and rather requires disclosure to clients of material interests, transactions, relationships, and other information, along with conflicts of interest policies, Nasdaq believes that the Proposal is a reasonable solution to enhance the integrity of proxy advisory reports. We agree with the Commission that voting decisions would be better informed if investors received sufficient information for them to understand and assess conflicts of interests and measures taken to address them.³⁰

The Commission notes that certain activities and relationships of proxy advisors may affect the objectivity and reliability of their proxy voting advice.³¹ Over the past decade, public companies have voiced similar concerns that potentially conflicting commercial relationships with companies and shareholders cause grave harm to companies and investors.³² Despite the Commission's commendable recent actions in this area, these concerns have not abated. Nasdaq continues to hear from companies that they are concerned with proxy advisors providing voting advice to clients on proposals while at the same time soliciting companies for corporate consulting services on those same proposals. One Nasdaq-listed company described this process as a "shakedown". It hired ISS to help calibrate its equity compensation plan according to ISS guidelines, and ISS then recommended voting against the plan and offered to recalculate the plan if the company would pay it to do so.³³ Statistics show that this is not an isolated example. In the 2019 Chamber Survey, 58% of issuers reported that they have been approached by the corporate consulting arm of ISS in the same year that the company received a negative vote recommendation.³⁴ Conflicts of interest are also inherent in the business model of Glass Lewis. It is partially owned by Ontario Teachers' Pension Plan and Alberta Investment Management Corp., both of which invest in companies on which Glass Lewis makes recommendations. This concern is compounded by the fact that Glass Lewis does not share draft reports with companies.³⁵

Former Commission Chairman Pitt publicly highlighted the perverse financial incentives that

²⁷ See Proposal at 30.

²⁸ Id.

²⁹ See Nasdaq 2013 Petition and Nasdaq 2013 Public Company Letter. Nasdaq noted that the Commission addressed transparency and conflict of interest concerns similar to those discussed herein in the context of credit rating agencies. In the case of credit rating agencies, as required by Dodd Frank, the Commission proposed rules governing the disclosure of conflicts of interest and credit rating methodologies.

³⁰ See Proposal at 29.

³¹ See Proposal at 27.

³² See Nasdaq 2013 Petition and 2013 Public Company Letter.

³³ See Appendix A, Company 2.

³⁴ See 2019 Chamber Survey at 12.

³⁵ See Nasdaq 2013 Petition.

often lurk behind these recommendations. In his prepared testimony on behalf of the U.S. Chamber of Commerce before a subcommittee of the House Committee on Financial Services on June 5, 2013 in which he criticized ISS and Glass Lewis for recommending a “say on pay” vote every year, irrespective of a particular company’s compensation practices, he noted that “[a]part from the utter waste and meaninglessness fostered by the ironclad ISS/Glass Lewis position on this issue, the one-year cycle they vigorously recommended, by definition, means that most, if not all, of the two firms’ institutional portfolio manager clients will need to retain ISS and Glass Lewis to fulfill their obligation to vote yearly on executive compensation.”³⁶

These concerns have increased in recent years.³⁷ In the 2019 Chamber Survey, nearly twice as many companies identified conflicts of interest at proxy advisors in 2019 than in 2018. Of companies surveyed, 19% identified significant conflicts of interest, up from 10% in 2018. While 16% of those companies that found conflicts brought them to the attention of institutional investors, a smaller number brought them to the attention of Commission Staff (7%) and the proxy advisors themselves (8%).³⁸ Retail investors are also concerned with conflicts of interest. The 2019 Spectrem Group Survey found that 78% of retail investors support requiring proxy advisors to disclose conflicts of interest.³⁹

While Nasdaq supports the Commission’s proposed approach and believes it promotes transparency and consistency, it appreciates the Commission’s willingness to consider alternatives that may finely tune the Proposal. In Question 16 of the Proposal, the Commission asks: “Should proposed Rule 14a-2(b)(9)(i) be more prescriptive regarding the presentation of conflicts of interest disclosure, or is it preferable to let the proxy voting advice business and its client determine how this information will be presented to the client?”⁴⁰ Nasdaq and 319 public companies have previously called for conflicts of interest to be disclosed on the front page of proxy advisor reports so that investors can make fully informed voting decisions.⁴¹ Standardizing the presentation of the disclosure will ensure that all clients have sufficient information to properly assess the objectivity and reliability of proxy voting recommendations. As such, Nasdaq believes the Commission should be more prescriptive regarding the presentation of conflicts of interest disclosure.

The Commission also asks whether it should “consider alternative thresholds or language for the proposed conflicts of interest disclosure.”⁴² Nasdaq has previously advocated for a principles-based materiality standard for public company periodic reporting requirements in recognition of the need to

³⁶ See *supra* note 14. See also David F. Larcker, Allan L. McCall and Gaizka Ormazabal, *The Economic Consequences of Proxy Advisor Say-on-Pay Voting Policies* (July 2012), available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2101453.

³⁷ Recently, Commissioner Roisman raised concerns that “certain asset managers get together and decide, for instance, that they do not like a particular member of a company’s board of directors. They then instruct the proxy voting advice business to recommend a vote against the director. The term I heard for this practice is ‘social arbitrage,’ a way for an asset manager to vote against a company, while maintaining its relationship with management so that it can sell products to that company such as providing 401(k) services.” Speech of Commissioner Elad L. Roisman, *Myths and Realities: Modernizing the Proxy Rules* (January 30, 2020), available at: <https://www.sec.gov/news/speech/roisman-myths-and-realities-2020-01-30>. See Appendix A, Company 10.

³⁸ See 2019 Chamber Survey at 12.

³⁹ See 2019 Spectrem Group Survey at 6 and 12.

⁴⁰ See Proposal at 37, Question 16.

⁴¹ See 2019 Public Company Letter.

⁴² See Proposal at 36, Question 14.

increase flexibility for companies to disclose material information to investors in an efficient and more shareholder-friendly manner.⁴³ Nasdaq supports the Commission's proposed materiality standard for conflicts of interest disclosure.

As noted above, SRD II requires each proxy advisor to publicly disclose certain information, including its conflicts of interest policy, code of conduct, and essential features of methodologies. The Commission should consider whether public disclosure of certain information, including the final voting reports and custom reports, would further protect investors and the public interest, promote transparency, and allow analysts and academic researchers to assess the impact of voting recommendations on a company's long-term value.

Review Period

In order to qualify for an exemption from the federal proxy rules, the Proposal would require proxy advisors to provide all companies with a review period of at least 5 business days (if the definitive proxy statement is filed 45 days or more before the shareholder meeting) or at least 3 business days (if the definitive proxy statement is filed 25-45 days before the shareholder meeting). We agree with the Commission that providing companies with an opportunity to review and provide corrections to draft voting recommendations would ultimately benefit investors by reducing the likelihood of errors, providing more complete information and improving the reliability of voting recommendations.⁴⁴

Nasdaq has previously advocated for proxy advisors to have a line of communication with the companies they analyze. We were joined by 319 public companies calling for the Commission to require transparent processes and practices that allow all companies, regardless of their market capitalization, to engage with proxy advisors on mistakes, inaccuracies and other significant disputes so that timely resolution of those disputes and corrections to the record can be made to minimize the negative impacts that such mistakes can have on the subject company's proxy voting outreach and its shareholders.⁴⁵ We were also joined by nearly 300 public companies in support of the draft review period provided under the Corporate Governance Reform and Transparency Act of 2017 (H.R. 4015).⁴⁶ The 2019 Spectrem Group Survey found that 79% of retail investors are in favor of a draft review process.⁴⁷

The current system is an uneven playing field. S&P 500 companies receive ISS voting recommendations in advance with a short window to suggest corrections to factual information,⁴⁸ whereas Glass Lewis does not provide draft reports at all.⁴⁹ In Nasdaq's own experience, we have been

⁴³ See Letter from John Zecca to Ms. Vanessa Countryman, Secretary, U.S. Securities and Exchange Commission, dated March 21, 2019, available at: <https://www.sec.gov/comments/s7-26-18/s72618-5177722-183507.pdf>.

⁴⁴ See Proposal at 44.

⁴⁵ See 2019 Public Company Letter.

⁴⁶ Letter from Nasdaq et. al. to The Honorable Paul Ryan and The Honorable Nancy Pelosi, dated December 15, 2017, available at: <https://www.nasdaq.com/docs/Proxy-Advisory-Support-Letter%20December-2017.pdf>.

⁴⁷ See 2019 Spectrem Group Survey at 15.

⁴⁸ See Nasdaq 2013 Petition.

⁴⁹ During Nasdaq's 2020 Issuer Outreach, one listed company shared that Glass Lewis recently approached it with an opportunity to submit feedback about Glass Lewis' analysis of their proposals, and have those comments distributed directly to Glass Lewis' investor clients. However, the company was told that to be

provided with as little as 24 hours to provide feedback on ISS voting recommendations, and requests to correct factual errors such as a director's age have been rejected. Factual errors have also been identified by 95% of Business Roundtable members and "all raise concerns regarding the rigor and integrity of the proxy advisory firms' internal fact-collection and analysis processes now hidden from public view."⁵⁰ The stories we hear from public companies further bear this out. We heard from one company that, in two successive years, a proxy advisor based its recommendations on an erroneous and incomplete understanding of the relevant facts. In each instance, the company was told that it could avoid some such issues by subscribing to (and paying for) the proxy advisor's corporate consulting services.⁵¹

There is a risk that shortcomings in the current fact-collection and analysis process could result in similar mistakes and inaccuracies in custom reports produced by proxy advisors. The 2019 Spectrem Group Survey found that 77% of respondents were at least slightly concerned that ISS "produces secondary or "specialty" reports that potentially contain conflicting vote recommendations from ISS's core benchmark report."⁵² The Commission should consider mitigating this risk by extending the proposed review and feedback process to custom reports.

Nasdaq believes that the Proposal would level the playing field by requiring all proxy advisors to provide a standardized review period to all companies, regardless of size. The ability to identify and correct errors is crucial for accuracy and accountability. Nasdaq supports this aspect of the Proposal and believes that most companies, including Nasdaq, would take advantage of this option, because notice and access requires a proxy statement to be filed 40 days before the annual shareholder meeting.⁵³

Nasdaq recognizes that a draft review process may raise confidentiality concerns because proxy advisors may consider certain information contained in proxy voting advice to be proprietary. The proposed rule permits a proxy advisor to require a company to enter into a confidentiality agreement before reviewing its draft report. While Nasdaq agrees with the Commission's proposal, Nasdaq asks the Commission to consider requiring each proxy advisor to file one standard form of confidentiality agreement with the Commission for review and approval, and each agreement entered into thereafter must follow that form. Nasdaq believes that standardizing and streamlining this process would promote transparency and efficiency by allowing companies to focus on substantive rather than procedural aspects during the review period. It would also reduce legal costs and time spent negotiating each confidentiality agreement and help ensure that such agreements contain standardized restrictions and disclaimers. We consistently hear concerns from our listed companies and companies considering accessing the public markets about the increasing compliance costs and regulatory burdens faced by public companies. The review process should not impose additional legal fees or other expenses on companies that make the process cost prohibitive.

eligible, it would need to purchase its annual report from Glass Lewis, and pay a fee of \$2,000 for its statement. See Appendix A, Company 7.

⁵⁰ See Letter from the Business Roundtable to Ms. Vanessa Countryman, Acting Secretary, U.S. Securities and Exchange Commission, dated June 3, 2019, available at: <https://www.sec.gov/comments/4-725/4725-5619758-185567.pdf>.

⁵¹ Nasdaq 2018 Roundtable Letter.

⁵² See 2019 Spectrem Group Survey at 6 and 12.

⁵³ See Proposal at 61, Question 26.

Hyperlink to Company-Provided Statement

In order to qualify for an exemption from the federal proxy rules, a proxy advisor would be required to provide a company with a copy of its final voting advice two days prior to publication and, if requested, include in its report a hyperlink to the company's response to its voting advice. Nasdaq agrees with the Commission that the proposed amendment would improve the overall mix of information available to investors by presenting the company's views in an efficient and timely manner.⁵⁴ We believe that it is important for each company to have the opportunity to present investors with its perspective because the Proposal does not require proxy advisors to revise their voting recommendations based on the company's feedback. The hyperlinked statement could also serve as a resource for investment advisors to become aware of "potential factual errors, potential incompleteness, or potential methodological weaknesses in the proxy advisory firm's analysis."⁵⁵ The Commission should consider whether it would be a breach of fiduciary duty for an investment advisor to make its voting determination without reviewing the company's statement.

The 2019 Spectrem Group Survey found that 75% of retail investors support the proposed hyperlink rule.⁵⁶ During Nasdaq's 2020 Issuer Outreach, we learned that most companies would take advantage of this option, particularly those who have received a negative recommendation due to "overboarding." The Commission notes that the company's response would be considered a "solicitation" required to be filed with the Commission and would be subject to the proxy antifraud prohibition of Rule 14a-9.⁵⁷ Nasdaq asks the Commission to consider amending the list of examples in the Rule 14a-9 to include items that companies may need to disclose to avoid violating the rule to prevent companies from being inadvertently tripped up.

Antifraud Rules

The antifraud provisions of Rule 14a-9 prohibit any proxy solicitations, including those exempt from the information and filing requirements of the federal proxy rules, from containing or omitting any materially false or misleading statements. Currently, Rule 14a-9 includes a list of examples of what may be misleading.⁵⁸ The Commission is proposing to amend this list to include additional examples of information that a proxy advisor would need to disclose in its proxy voting advice to not be misleading, such as its "methodology, sources of information, conflicts of interest or use of standards that materially differ from relevant standards or requirements that the Commission sets or approves."⁵⁹ We agree with the Commission that the amendments are in the public interest, promote investor protection, and help ensure that investors are provided the information they need to make fully informed voting decisions.⁶⁰

⁵⁴ See Proposal at 53.

⁵⁵ See Question and Response 4 of *Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers*, Release No. IA-5325 (Aug. 21, 2019) [84 FR 47420 (Sept. 10, 2019)].

⁵⁶ See 2019 Spectrem Group Survey at 6.

⁵⁷ See Proposal at 54.

⁵⁸ These are: predictions as to specific future market values; material which directly or indirectly impugns character, integrity or personal reputation, or directly or indirectly makes charges concerning improper, illegal or immoral conduct or associations, without factual foundation; failure to so identify a proxy statement, form of proxy and other soliciting material as to clearly distinguish it from the soliciting material of any other person or persons soliciting for the same meeting or subject matter; and claims made prior to a meeting regarding the results of a solicitation. See Proposal at 69.

⁵⁹ See Proposal at 141.

⁶⁰ See Proposal at 68 and 73.

Nasdaq has long advocated for increased transparency around the models, methodologies and voting policies used by proxy advisors. In 2013, Nasdaq petitioned the Commission to require proxy advisors to publicly disclose the models, formulas and methodologies pursuant to which they evaluate and make recommendations regarding how shareholders should vote on matters presented to them for a vote.⁶¹ This petition was supported by 58 public companies.⁶² In 2019, Nasdaq was joined by 319 public companies voicing concern that proxy advisors “significantly affect voting recommendations using opaque rules, which require paid services to interpret. Moreover, in the absence of transparent policies, neither the proxy advisory firms’ clients, nor the companies they report on, can determine whether a policy is applied correctly or if a recommendation is based on factual errors.”⁶³ As noted above, SRD II requires proxy advisors to publicly disclose, among other things, “the essential features of the methodologies and models they apply; the main information sources they use;...whether and, if so, how they take national market, legal, regulatory and company-specific conditions into account; the essential features of the voting policies they apply for each market.”⁶⁴

The 2019 Spectrem Group Survey found that 79% of retail investors are concerned with a lack of sufficient transparency in voting policies and procedures.⁶⁵ This concern is compounded with the risk of unpredictable changes to voting policies that catch companies off guard. For example, a proxy advisor may issue a new voting policy in October 2019 that applies to a calendar-year company’s policies and actions from January 1, 2019, subjecting the company to retroactive criteria that are impossible to satisfy. Changes to policies or criteria should only apply to companies’ fiscal years beginning after that date.

While the Proposal does not call for public disclosure of models and methodologies, Nasdaq believes that including disclosure in the voting advice will promote transparency. Currently, relatively little is known about the policies and methodologies used by proxy advisors. Companies and academics have noticed that proxy advisors use a “one-size-fits-all” approach that disregards the specific circumstances of a company or industry. Former Commissioner Troy A. Paredes noted that such “one-size-fits-all governance and pay practices [of proxy advisory firms] don’t work so well for most companies.”⁶⁶ For example, proxy advisors oppose classified boards for all companies, but “research shows quite plainly that the impact of a staggered board is not uniformly positive or negative.”⁶⁷ The 2019 Spectrem Group Survey found that 93% of retail investors believe that a company-specific analysis, rather than a one-size-fits-all approach, should be an important element of proxy advisory voting recommendations.⁶⁸

Nasdaq appreciates the Commission’s consideration of additional measures to further increase transparency. The Commission seeks comment on whether the list of examples in Rule 14a-9 should

⁶¹ See Nasdaq 2013 Petition.

⁶² See 2013 Public Company Letter.

⁶³ See 2019 Public Company Letter.

⁶⁴ See *supra* note 24.

⁶⁵ See 2019 Spectrem Group Survey at 13.

⁶⁶ See *supra* note 14.

⁶⁷ David F. Larcker and Bryan Tayan, “Loosey-Goosey Governance: Four Misunderstood Terms in Corporate Governance,” *Stanford Closer Look Series* (October 7, 2019), available at: <https://www.gsb.stanford.edu/sites/gsb/files/publication-pdf/cgri-closer-look-79-loosey-goosey-governance.pdf>.

⁶⁸ See 2019 Spectrem Group Study at 14.

include standards that materially differ from those of other regulators, such as state or foreign regulators, in addition to those set or approved by the Commission.⁶⁹ In Nasdaq's own experience, ISS has determined that a director was not independent under its criteria even though the director was independent under Nasdaq and SEC rules. Nasdaq asks the Commission to require proxy advisors to also disclose if their standards materially differ from those of the stock exchange that the company is listed on. Unlike proxy advisors, the rules of stock exchanges are subject to a public notice and comment period and the Commission must find that those rules protect investors and the public interest.⁷⁰ Nasdaq and other listing exchanges must also publish their rules and any stated policy, practice or interpretation, which promotes transparency.

Conclusion

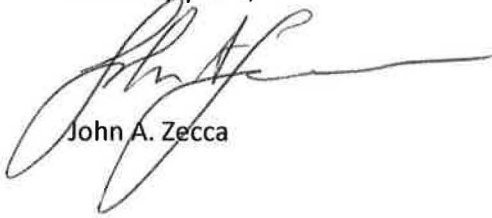
Nasdaq believes that investors, issuers and other market participants will benefit from healthy capital markets that promote trust and transparency. Nasdaq supports the Commission's Proposal to require transparency about the methodologies and conflicts of proxy advisory firms, as well as a mechanism for companies to address errors by these firms. Nasdaq recognizes that proxy advisors provide important research on public companies and can streamline the voting process for institutional investors. We commend the Commission for weighing these important considerations against the calls for increased transparency, accuracy and accountability voiced by Nasdaq, Nasdaq-listed companies, Congress, academics, retail investors and the press over the past decade.

⁶⁹ See Proposal at 73, Question 54.

⁷⁰ 15 U.S.C. 78f(b)(5).

Thank you for your consideration of our comments. Please feel free to contact me with any questions.

Sincerely yours,

A handwritten signature in black ink, appearing to read 'John A. Zecca', with a long horizontal flourish extending to the right.

John A. Zecca

Appendix A

2020 Issuer Outreach

Appendix A

Company 1

An employee* of mid-cap issuer in the financial services industry notes that ISS utilizes a three year shareholder return computation based upon December 31 stock prices. This may disadvantage companies with smaller float with stock prices which trade in a wider range.

ISS utilizes a proprietary model to determine the number of shares which can be offered in an equity plan. However, a subscription is required to access the computation for allowable shares. This places undue pressure on companies to buy a subscription. ISS guidelines for this should be public and not require the payment of a fee set by ISS.

ISS does not permit companies to contact analysts to correct misconceptions or errors. Instead it requires additional clarifying public filings which involves extra expense and can cause confusion.

A significant improvement is to give companies a 5 day period to correct errors and misconceptions and require that those responses be included in the ISS report.

The real solution is that the ISS advisory service change its name and become completely disassociated with the same company which issues voting recommendations. Otherwise there will be a permanent conflict of interest. Shareholder advisory services perform a valuable function and they should be beyond reproach and should not be conflicted. If the elimination of that conflict of interest is not feasible, then companies should have the capability of correcting ISS recommendations at the time they are issued as suggested above.

*Note: The individual who has submitted these observations has requested that they be noted as representing his personal opinions and experiences with ISS and that he is not speaking in an official capacity.

Company 2

A mid cap medical devices company described ISS's issuer outreach tactics as a "shakedown". One year, the company included a shareholder proposal to increase the number of units available for its equity compensation plan. ISS does not publicly disclose the calculation used to determine whether the number of units under an equity compensation plan are appropriate, so the company hired ISS's consulting group to calculate the appropriate number based on the factors and variables considered by ISS's rating group. The company calibrated its plan based on ISS's feedback, yet after the company filed its proxy statement, ISS recommended a vote against it. ISS then approached the company and offered to recalculate the plan if the company would rehire them to do so. The company declined and worked with a proxy solicitor to help communicate the merits of the units asked for in the shareholder proposal, which cost a significant amount of money and time. A company executive spent a lot of hours personally with shareholders trying to convince them to vote for the plan despite ISS' recommendation and noticed that many shareholders will vote however ISS recommends as a safe harbor. Eventually the plan passed its shareholder vote by a thin margin. Every year ISS tries to sell its services to the company for say on pay and general compensation. The company feels that the industry is monopolized by ISS and Glass

Lewis without any checks and balances and believes the proposal is a positive step forward but may not completely eliminate this behavior.

Company 3

A software company with a single majority shareholder is contacted by ISS consulting services every quarter in attempts to sell its services. The company is concerned that ISS may be biased due to conflicts of interest and use a one-size-fits-all model without regard to company-specific situations. ISS has opposed the company's dual class structure and staggered board, which the company views as critical to maintaining a long term vision for the company. The company fears that if not for its majority shareholder, it would feel pressured to adjust its governance structure in response to the influence exerted by proxy advisors. The company welcomes the proposed changes and encourages the SEC to swiftly implement them.

Company 4

A small cap industrial company does not receive drafts of ISS voting recommendations in advance and has discovered errors after the report is issued. In one case, ISS recommended voting against all of the company's directors as a result of an egregious error. When the company notified ISS of the error, ISS attributed the mistake to information it received from Equilar and refused to correct it. The company then had to conduct a major outreach effort to inform its institutional investors of the error so that they would not oppose the proposal. The company believes the SEC's proposed draft review process is a critical and common sense solution that will increase the accuracy of proxy voting reports. The company also supports the proposal to include a hyperlink to a company-provided statement in the proxy voting report so that companies can tell their side of the story, especially if the proxy advisor has refused to correct an error.

The company disagrees with the one-size fits all approach used by proxy advisors, particularly related to compensation plans, staggered boards and poison pills. The company believes a poison pill may be appropriate for a smaller market cap company like itself but ISS does not take company-specific conditions into account. The company has terminated a poison pill because ISS recommended voting against it, but keeps a poison pill "on the shelf" that can be quickly implemented if it receives an unsolicited bid. The company believes that this is not in the best interest of shareholders because the "shelf" poison pill is not publicly disclosed to shareholders. The company has heard that this is common practice among companies that have received a negative recommendation against a poison pill by a proxy advisor.

The company has recently received new ESG scores from ISS. The scores were low because the company's public disclosure about its ESG practices did not conform with ISS's guidelines. The company is concerned that there is a lack of transparency around these guidelines and the calculation of the new ESG metric, and is also concerned that the cost of preparing disclosures that meet ISS requirements is particularly burdensome for smaller public companies.

Company 5

A financial services company is concerned that the proxy advisory industry is a deeply conflicted duopoly. ISS and Glass Lewis sell to both sides of the street—they will rate companies on corporate governance practices based on a black box model with little transparency based on information that is

proprietary to them and tweaked without notice year after year, and then turn around and offer corporate consulting services to help pass black box hurdles that only they have the full details of. The company likened the conflict to an educational test services company offering the SAT and also providing the only prep courses for the SAT. The company feels pressured to hire ISS' consulting services every year because there is no clear set of guidelines to follow. The company supports the SEC's proposal to require disclosure of models and methodologies.

The company believes that large asset managers rely on proxy advisors because they have to vote thousands of proxies every year and do not have the time or resources to independently evaluate each proposal. It is therefore critical for reports to be accurate and reliable. When a proxy advisor is giving a rubber stamp of disapproval on corporate governance practices and not being held accountable for its errors, the company is required to amend its proxy statement to explain such errors because there is no effective way to interact with the proxy advisor in the current system. The company supports the SEC's proposed draft review period.

The company is concerned that proxy advisors use one-size fits all policies. For example, as a financial services company, it pays bonuses on a discretionary basis, whereas other companies in other industries may pay out bonuses based on a pre-established formula. The company has noticed that proxy advisors do not make adjustments for practices common in its industry.

Overall, the company supports holding proxy advisors accountable for their voting decisions. This isn't about free speech, this is about fiduciary duties.

Company 6

A small cap software company is concerned that ISS' policies regarding overboarding may be black and white with no room for nuance, discussion or presenting the company's point of view. In the past, ISS has recommended voting against a director who is also the chief executive officer of one of the company's significant shareholders because the director also sits on boards of 3-4 other public companies in which his entity holds a significant equity interest. While this model is common for private equity firms, it does not fit into ISS's black and white policy. The company supports the SEC's proposal to require proxy advisors to include a hyperlink in its voting advice so that the company can tell its story. This would allow the company to explain to its investors that there is a valid reason for its director to sit on several boards and that he and the company's retail shareholders share a common interest in stock appreciation and company value.

An executive of the company also shared his personal experience with a prior company. That company went into bankruptcy and as a condition to emerging from bankruptcy, it filed a Form 10 to list on an exchange. The bankruptcy court approved its stock plan as agreed to by the company's creditors and debtors committees in accordance with bankruptcy law. The company was required in its first annual meeting to propose an evergreen increase to the stock plan in its proxy statement. ISS contacted the company and said that because the original plan was not approved by shareholders, they would recommend voting against all compensation committee members. The company tried to explain that the plan was approved by bankruptcy court when the company didn't have any shareholders and was not even listed on an exchange. ISS did not adequately explain why their shareholder approval provisions would even apply given that the plan was not subject to shareholder approval pursuant to applicable bankruptcy laws. The company had to revise the plan to fit within ISS' narrow guidelines and then propose it to shareholders when such approval was not required by law. During the company's

outreach to institutional investors, investors told the company that they were bound by their internal policies to vote in accordance with the proxy advisor's recommendations. The company is also supportive of the SEC's proposal to disclose methodologies and conflicts of interest.

Company 7

A large cap company supports the SEC's proposal and is particularly concerned with a lack of transparency and conflicts of interest. The company noted that investors are increasingly focused on ESG, and it is in turn a focus point for the management and board. ISS recently introduced a new ESG score on the ISS platform following its acquisition of oekom research AG, a European ESG ratings provider. The company now has two ESG scores based on two methodologies--a quality score, which appears to be focused on its disclosure and can be updated in real time using the ISS platform, and an "oekom score", which aims to evaluate the company's ESG performance but is based on outdated information that cannot be updated on the ISS platform. The company proactively reached out to ISS to try to better understand the score but instead, ISS used it as an opportunity to sell additional governance services and the company was told to separately reach out to oekom directly for more details. The company has experienced pressure tactics like this in the past with ISS' compensation offerings. In terms of compensation-related equity plans, the company believes that most issuers are forced to purchase such services from ISS because plans will be evaluated against ISS's model, which will determine whether ISS recommends voting in favor of it.

ISS typically provides the company with 48 hours to review its draft proxy research report. Historically, the company has had little success correcting simple, year-over-year factual errors (that can be easily verified through the company's proxy disclosure) in successive voting reports, despite repeated attempts to do so. Correction required an off-season engagement request involving senior management and directors from the company's board. In addition, while this review period is afforded to issuers in an uncontested setting, this is not the case in contested situations. When the company found itself in a contested situation with respect to one of its proposals, there was no opportunity to review the voting report (on any matter up for a shareholder vote, not just the contested piece) before it was issued.

While ISS ultimately provides a complimentary copy of its proxy research report to the issuer, Glass Lewis requires purchase of its proxy research report. The company was also approached by Glass Lewis in recent months in connection with its "Report Feedback Statement" ("RFS") service which purportedly enables the subjects of Glass Lewis' proxy research to submit feedback about the analysis of their proposals, and have those comments distributed directly to Glass Lewis' investor clients. However, the company was told that to be eligible for the RFS program, it would need to purchase its annual report from Glass Lewis, and pay an RFS fee of \$2,000 for its statement. Therefore, the company supports the SEC's proposal to require proxy advisors to include a hyperlink to the company's response to the voting recommendations. The company believes that because it would be considered a solicitation, companies would be cautious about what is included in their statement, and filing such a statement with the SEC would not be tremendously burdensome.

Company 8

An industrial and energy company spends an inordinate amount of money and time due to ISS and Glass Lewis. The company constructed a compensation structure that it believed incentivized employees,

however, due to pressure exerted by proxy advisors, it amended its compensation plan in order to avoid a negative recommendation. The company is also concerned that the methodologies of proxy advisors are not transparent. One year ISS recommended voting against its say on pay proposal, whereas Glass Lewis recommended voting for it. The company spent an inordinate amount of time reaching out to institutional investors to explain management's view on the proposal. The company also believes that proxy advisors do not understand their business—the company uses long term metrics unique to the industries it operates in, whereas proxy advisors use short term metrics that offer no value or insight to shareholders. The company is particularly concerned with the new Economic Value Added (EVA) metric that ISS began using in the same year it acquired EVA Dimensions LLC. This new metric required the company's compensation committee to spend additional time on new calculations used only by ISS.

Due to the retrospective view of proxy voting advice, the company believes proxy advisors do not present investors with sufficient detail regarding changes that will affect future years. Last year, the company made three complex changes to its compensation program in response to specific feedback it heard from investors that would be effective going forward. However, the proxy advisor only included one short sentence about the changes, leaving investors without sufficient information.

The company has consistently (each year) spent money on a compensation consultant to help it predict proxy advisor's voting recommendations, though its predictions are not consistently accurate. The company has also paid approximately \$5,000 to review a proxy advisor voting report and heard that if you hire ISS's consulting arm for \$40,000 a year, it will give you insight into its methods, analyze your numbers and provide you with confidence in what its voting recommendation will be. The company has declined to engage its consulting arm because it believes this is an inherent conflict of interest. Recently, the company learned that it will no longer be able to obtain Glass Lewis' research and recommendations on North America through Equilar and will have to pay Glass Lewis directly instead (specific message from Glass Lewis: "As you're aware, Glass Lewis has announced significant changes to its Pay-for-Performance Model and Peer Group methodology for the 2020 proxy season, which are not available via Equilar, and are part of our new exclusive partnership with CGLytics to provide governance and compensation data.")

Company 9

A mid-cap company, with global operations, supports the SEC's proposal. The company views proxy advisory firms as external contingencies that place pressure on the company to adopt corporate governance practices that may not be in the best interest of the company or its shareholders. The company constructed an executive compensation package that was based on the achievement of long-term goals. However, ISS recommended voting against say on pay because it did not fall within ISS' guidelines. The company hired a compensation consulting firm to adjust its executive compensation plan in order to obtain a favorable voting recommendation from ISS. In addition, the company felt pressured to subscribe to ISS' corporate governance solutions services. The company believes that this has increased the cost of being a public company.

The company has also had to react to ISS recommendations on "overboarding," for which ISS follows a rigid one size fits all criteria.

The company is concerned that ISS' methodologies are opaque and can change without notice. The company receives a monthly ESG score from ISS that can fluctuate from month to month even if the company's practices and policies remain the same. The company is not provided visibility into the basis

for these score changes, other than because other companies in its peer group have implemented changes that improve their score and worsen the company's score. In addition, ISS has adjusted its scope and methodology several times, adding new scores and new measurement techniques with limited input from the companies it is reviewing. The company believes that it would benefit from increased transparency around the methodologies used by ISS.

The company has never been given the opportunity to review and comment on a draft ISS report in advance and welcomes the SEC's proposal to extend this to all companies.

Company 10

A large cap diversified company was reluctant to issue its own comment letter in response to the SEC's proposal due to fear of retribution from proxy advisors and shareholder proponents. The company is particularly concerned with company proposals, including say on pay, where the proxy advisors demonstrate a lack of knowledge of the company and do not conduct a thorough analysis before issuing their voting recommendations. One year, Glass Lewis recommended against the company's say on pay proposal in part because of a certain practice that the company allegedly followed. The company has never followed that practice. Glass Lewis did not share the draft report with the company in advance, and the company had to purchase the report after it was issued to even view it. Once the company pointed out the error to Glass Lewis, it corrected it and reissued the report. This error would have gone unrectified if the company had not paid for the report and proactively reached out to Glass Lewis.

Another year, ISS issued a voting recommendation on a certain proposal. Shortly thereafter, ISS modified commentary around its recommendation and resissued the report. It is unclear whether the modifications were made based upon further ISS internal review or influence from an outside investor.

The company believes that ISS's compensation analysis may be skewed due to the way it constructs a company's peer group, which may differ from the way the company and its compensation consultant constructs its peer group. For example, ISS has included in its peer group a large cap company that doesn't pay its executive any cash compensation, whereas the company does. The company is concerned that proxy advisory firm methods lack transparency and may use a one-size-fits-all model that disregards company-specific factors. The company asks the SEC to consider requiring proxy advisors to include in their reports an excerpt of the company's proxy statement related to compensation alongside the proxy advisor's analysis so that investors can see both sides of the story, similar to what proxy advisors generally do currently for shareholder proposals.

Appendix B

2019 Chamber Survey

2019

PROXY SEASON SURVEY



CENTER FOR CAPITAL MARKETS
COMPETITIVENESS



2019

PROXY SEASON SURVEY

Presented by:



CENTER FOR CAPITAL MARKETS
COMPETITIVENESS

Fundamental components of the U.S. capital markets are strong corporate governance laws and regulations that promote long-term shareholder value and encourage businesses to enter the public markets. When more businesses elect to go public, job creation accelerates and Main Street households are provided with greater opportunities to build and sustain wealth.

Regrettably, the past two decades have witnessed a steady decline in the number of U.S. public companies. There are now roughly half the number of public companies than existed 20 years ago, and the initial public offering (IPO) market remains a fraction of what it was in the latter part of the 20th century. This presents significant challenges to long-term economic growth and the ability of Main Street households to invest in successful American businesses.

Congress and the Securities and Exchange Commission (SEC) have taken actions in recent years to help stem this decline and make the public company model attractive again for entrepreneurs. The 2012 Jumpstart Our Business Startups (JOBS) Act scaled regulation for small issuers, and the recent agenda of the SEC has prioritized disclosure reform, expansion of certain provisions of the JOBS Act, and other initiatives intended to right-size regulation and encourage more businesses to complete an IPO.

One issue of increasing interest to policymakers is the outsized role that proxy advisory firms play in corporate governance and the challenges these firms pose to businesses that are already public or considering an IPO. While proxy advisory firms exist to provide institutional investors with analysis and vote recommendations for various proxy issues, past regulatory actions have helped the firms “control” a significant portion of the vote at public companies. As a result, many public companies—particularly small and mid-size issuers—are left to the mercy of decisions made by proxy advisory firms.

The proxy advice market is dominated by two firms—Institutional Shareholder Services (ISS) and Glass Lewis—which collectively control 97% of the industry. ISS and Glass Lewis have effectively become the standard setters for corporate governance in the United States, notwithstanding the fact these firms have a history of making errors, are rife with conflicts of interest, and provide little transparency as to how they develop vote recommendations.

This is the fifth year that Nasdaq and the U.S. Chamber of Commerce have conducted a survey to examine the experiences public companies had with proxy advisory firms during the most recent proxy season. The survey is intended to help inform current and future regulatory initiatives related to proxy advisory firms and their role within the U.S. proxy system.

BACKGROUND

The practices and influence of proxy advisory firms have become an increasing topic of interest among policymakers over the past decade. Republicans and Democrats in Congress, as well as the SEC, have expressed concern over deficiencies within the industry, including

- a track record of making errors or misjudgments in analysis when developing vote recommendations, a flaw that ultimately misinforms investors and impairs voting decisions on proxy issues at public companies;
- a startling lack of transparency that leaves market participants guessing as to how ISS and Glass Lewis formulate voting advice;
- significant conflicts of interest that have the potential to taint voting recommendations and introduce biases into the voting process; and
- a “one-size-fits-all” approach that does not produce company-specific analysis or vote recommendations and instead applies uniform policies to nearly every public company.

In 2013—following the release of a report by the Chamber on best practices for the proxy advice industry—the first congressional hearing on proxy advisory firms was held.^{1 2} Later that year, the SEC held a public roundtable to examine the use of proxy advisory firms by institutional investors and investment advisers. While Nasdaq was on record in 2013 with its own concerns about the behavior of proxy advisers, in May 2017, Nasdaq made proxy advisory reform a cornerstone of its blueprint to revitalize the capital markets.³

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1. Best Practices and Core Principles for the Development, Dispensation, and Receipt of Proxy Advice. (March 2013) Available at <http://www.centerforcapitalmarkets.com/wp-content/uploads/2010/04/Best-Practices-and-Core-Principles-for-Proxy-Advisors.pdf>
 2. “Examining the Market Power and Impact of Proxy Advisory Firms” Subcommittee on Capital Markets and Government Sponsored Enterprises (June 5, 2013).
 3. The Promise of Market Reform Reigniting America’s Economic Engine (May 2017). Available at https://www.nasdaq.com/docs/Nasdaq_Blueprint_to_Revitalize_Capital_Markets_April_2018_tcm5044-43175.pdf

As a result of this public concern, SEC staff issued Staff Legal Bulletin 20 (SLB 20) in 2014 to provide guidance to investment advisers regarding their voting obligations under the Proxy Voting Rule, and to clarify the circumstances under which proxy advisory firms can obtain an exemption from the SEC's proxy solicitation rules.⁴ Importantly, SLB 20 reiterated that the fiduciary obligation of investment advisers permeates all aspects of proxy voting, including when investment advisers engage a proxy advisory firm for analysis and vote recommendations.

While the issuance of SLB 20 was a positive development, there are limitations as to the impact that staff-level guidance can have in practice. Congress therefore felt the need to become further involved as it considered legislation related to proxy advisory firms. In December 2017, the House of Representatives passed bipartisan legislation—H.R. 4015, the Corporate Governance Reform and Transparency Act—that would require proxy advisory firms to register with the SEC and become subject to an oversight and examination regime. Subsequent legislation introduced in Senate demonstrated there was a bipartisan and bicameral consensus that the regulatory status quo for proxy advisers needed to be changed.⁵

Over the past 18 months, the SEC has responded to these concerns and taken action on its own to update the regulatory framework that applies to proxy advisory firms and the institutional investors that hire them:

- In September 2018, SEC staff withdrew two no-action letters that were issued to ISS and Egan Jones (another proxy advisory firm) in 2004.⁶ These letters received wide criticism for allowing institutional investors to outsource voting decisions to proxy advisers, thereby increasing the level of influence that proxy advisory firms hold over voting decisions.

4. Proxy Voting: Proxy Voting Responsibilities of Investment Advisers and Availability of Exemptions From the Proxy Rules for Proxy Advisory Firms (June 30, 2014). Available at <https://www.sec.gov/interps/legal/cfslb20.htm>.

5. S. 3614, the Corporate Governance Fairness Act (Introduced November 13, 2018 by Sens. Reed, Perdue, Heitkamp, Tillis, Jones, and Kennedy).

6. Statement Regarding Staff Proxy Advisory Letters—Division of Investment Management (September 13, 2018). Available at <https://www.sec.gov/news/public-statement/statement-regarding-staff-proxy-advisory-letters>.

- The SEC held a roundtable on the U.S. proxy system in November 2018 that included a lengthy discussion of proxy advisory firms and their impact on corporate governance.⁷ The SEC has also received hundreds of written comments related to the roundtable, including from issuers describing specific problems they have had with proxy advisory firms over the years. One of those submissions was a Nasdaq-coordinated letter, signed by over 300 companies and trade associations, calling on the SEC to take strong action to regulate proxy advisory firms.⁸
- In August 2019, the SEC issued Commission-level guidance (“Commission Guidance”) that built on SLB 20 and is intended to encourage reasonable due diligence by institutional investors when using proxy advisory firms, including taking steps to ensure that vote recommendations are based on sound analysis and data and are not tainted by conflicts of interest. The guidance also clarifies the circumstances by which proxy advisory firms are subject to the SEC’s proxy solicitation rules, and reiterates that even exempt solicitations are still subject to SEC rules that prohibit false or misleading statements.⁹
- In November 2019, the SEC proposed rules that condition proxy advisory firms’ exemptions from the proxy solicitation rules upon the firms meeting certain transparency and accountability requirements.¹⁰ For example, the proposal requires that proxy advisory firms disclose material conflicts of interest to their clients, provide issuers with opportunities to comment on vote recommendations to ensure accuracy, and include in final vote recommendations a hyperlink or other medium to an issuer’s viewpoint regarding the proxy issue at hand. These steps will promote more objective proxy vote recommendations and ensure that investors receive all information necessary to make informed voting decisions.

7. Spotlight on the Proxy Process (November 15, 2018). Available at <https://www.sec.gov/proxy-roundtable-2018>.

8. Letter available at <https://www.sec.gov/comments/4-725/4725-4872519-177389.pdf>.

9. Commission Interpretation and Guidance Regarding the Applicability of the Proxy Rules to Proxy Voting Advice (August 21, 2019). Available at <https://www.sec.gov/rules/interp/2019/34-86721.pdf> ; Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers (August 21, 2019). Available at <https://www.sec.gov/rules/interp/2019/ia-5325.pdf>.

10. Amendments to Exemptions From the Proxy Voting Rule for Proxy Voting Advice (November 5, 2019). Available at <https://www.sec.gov/rules/proposed/2019/34-87457.pdf>.

2019

PROXY SEASON SURVEY

The U.S. Chamber of Commerce’s Center for Capital Markets Competitiveness (CCMC) and Nasdaq partnered again to conduct a survey of public company experiences with proxy advisory firms during the 2019 proxy season. This is the fifth annual CCMC/Nasdaq proxy season survey and is intended to help policymakers and market participants understand how public companies engaged with proxy advisory firms, investors, and regulators throughout the most recent proxy season. A record 172 companies participated in the survey.

A notable finding from this year’s survey is that fewer issuers are requesting previews of vote recommendations or asking for opportunities to meet with proxy advisory firms on matters subject to a shareholder vote. This development has occurred at the same time proxy advisory firms are less likely than in previous years to grant such requests, leading several companies to believe that any attempt to correct factual errors or engage in substantive dialogue with proxy advisory firms is futile.

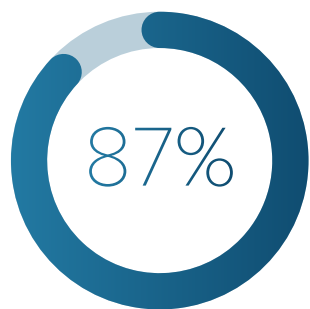
The survey also found—as did last year’s survey—that many companies report a significant portion of their shares are “robo-voted” by institutional investors within two days after an ISS or Glass Lewis vote recommendation is issued. Such automatic voting of shares has caught the attention of the SEC and Congress, and calls into question whether there is still an overreliance on proxy advisory firm recommendations.

The survey also highlights the increasing awareness that issuers have regarding conflicts of interest at proxy advisory firms. Nearly twice as many companies identified significant conflicts at proxy advisory firms, with some bringing them to the attention of institutional investors.

Notably, 58% of issuers reported that they have been approached by the corporate consulting arm of ISS in the same year that the company received a negative vote recommendation. As the Chamber, Nasdaq, and many others have long pointed out, the ISS business model—in which the company provides corporate governance consulting to the very issuers that it is issuing vote recommendations on—is inherently conflicted and creates the potential for biased voting advice. Regulators should be vigilant in ensuring that these conflicts ultimately do not harm investors, who rely on sound and objective voting advice to create long-term value.

SURVEY RESULTS

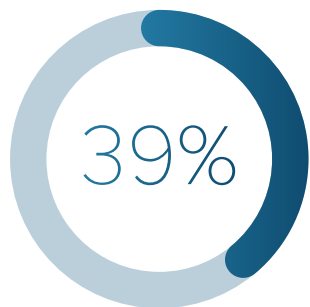
Corporate Engagement With Proxy Advisory Firms: Issuers Still Find It Difficult to Engage Constructively With Proxy Advisory Firms



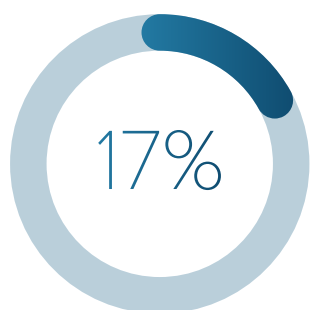
Of companies surveyed, **87% had a proxy advisory firm make a recommendation** on an issue included in their proxy statements, a level that is 5% lower than in 2017 and 2018.



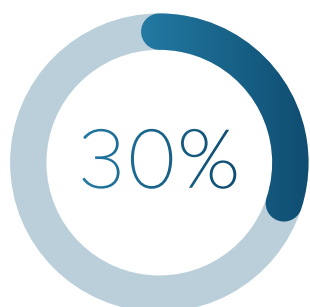
Of companies, **80% carefully monitored proxy advisory firm recommendations** for accuracy or reliance on outdated information, lower than in 2018 (83%) and 2017 (91%).



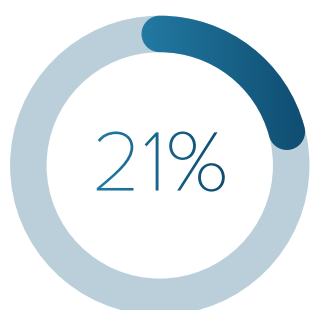
Of companies, **only 39% believed that proxy advisory firms carefully researched and took into account all relevant aspects of a particular issue** on which the firms provided advice, the same number as in 2018.



Of companies, **17% formally requested that proxy advisory firms provide them with a preview of vote recommendations**, down from 21% in 2018 and 30% in 2017. For companies that did request a preview, proxy advisory firms provided them only 39% of the time, down 5% from 2018.

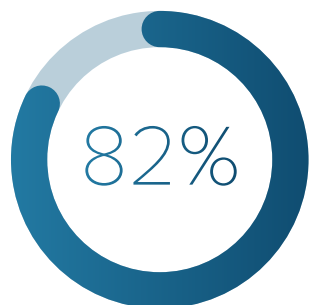


The number of companies asking proxy advisory firms for opportunities to provide input both before and after the firms' recommendations were finalized continues to decline. In 2019, **30% of companies made such requests**, down from 38% in 2018 and 51% in 2017. Once again, companies commonly reported that, if such a request was granted, they were often only given only one to two days (and sometimes only hours) to provide input.

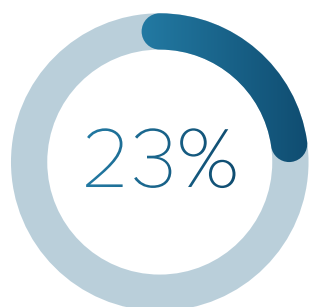


The number of companies pursuing opportunities to meet with proxy advisory firms on issues subject to shareholder votes also continues to decline. Of companies, **21% pursued meeting opportunities in 2019**, down from 29% in 2018 and 52% in 2017. For companies that asked for a meeting, their request was denied 60% of the time, a number that continues to grow from 2018 (57%) and 2017 (38%).

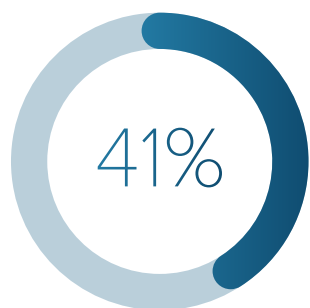
Issuer Engagement With Investors and the SEC



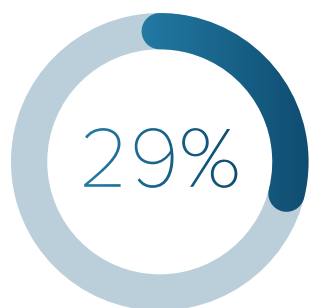
A large majority of companies still reported that they have some form of a year-round, regular communications program with institutional investors. Of issuers, **82% reported having such a program**, up from 78% in 2018. The companies that do regularly communicate with institutional investors throughout the year found such communication to be beneficial when it comes to proxy matters.



Companies that believed they were not granted adequate opportunities for input on a proposed proxy adviser vote recommendation **notified proxy adviser firms and portfolio managers 23% of the time**, a slight decline from 2018.

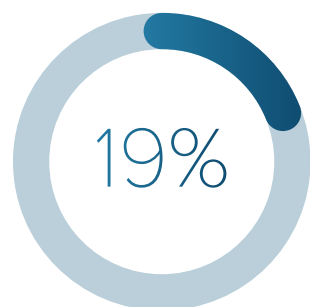


When companies encountered a vote recommendation they believed was based on inaccurate or stale data, they **alerted the proxy advisory firm, portfolio managers, and/or SEC staff 41% of the time**, a 5% decrease from 2018. Companies also reported making supplemental proxy filings with the SEC to alert the public to issues regarding the quality of vote recommendations or the process employed by the proxy advisory firms.

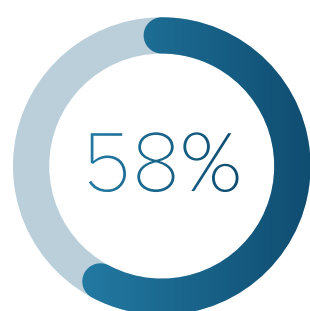


Of companies, **29% advised proxy advisory firms and their clients of recommendations that did not advance the best economic interest of shareholders**, a 10% decrease from 2018.

Conflicts of Interest a Rising Concern for Companies

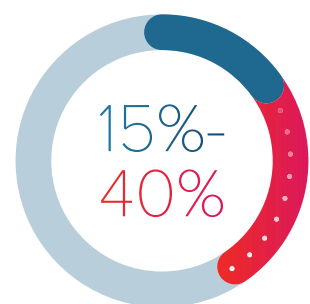


Nearly twice as many companies identified conflicts of interest at proxy advisory firms in 2019 than in 2018. Of companies, **19% identified significant conflicts of interest**, up from 10% in 2018. While 16% of those companies that found conflicts brought them to the attention of institutional investors, a smaller number brought them to the attention of SEC staff (7%) and the proxy advisory firms themselves (8%).



A striking **58% of companies reported being approached by ISS Corporate Solutions during the same year in which the company received a negative vote recommendation**. Of companies, 19% reported that they have hired ISS Corporate Solutions for advice on structuring executive compensation plans, improving ESG ratings, gauging proxy advisory outcomes, or other corporate governance matters.

Significant Percentage of Shares Voted in Line With Proxy Advisory Firm Recommendations



As in 2018, many issuers reported that a large percentage of their shares were robo-voted in the 24 to 48 hours after an ISS or Glass Lewis vote recommendation was released. When an ISS recommendation was issued, several companies reported that between 15% and 40% of their outstanding shares were voted in line with the recommendation within two days. The same issue arose with Glass Lewis, although on a smaller scale, with several companies reporting that between 5% and 10% of their shares voted automatically with a Glass Lewis recommendation.

PROXY ADVICE BEST PRACTICES

The three constituency groups affected by the recently issued SEC guidance—proxy advisory firms, portfolio managers, and public companies—must focus their attention on five overarching principles:

Fiduciary duty

Fiduciary duties permeate and govern all aspects of the development, dispensation, and receipt of proxy advice. Some investors use proxy advisory reports as one data point among many in an independent process to determine how or when they should vote their shares. Unfortunately, other investors may outsource their voting to proxy advisory firms without any due diligence.

Shareholder value

Enhancing and promoting shareholder value must be the core consideration in rendering proxy voting advice as well as making proxy voting decisions.

Freedom from conflict

The proper role of proxy advisory firms vis-à-vis proxy voting is to provide accurate and current information to assist those with voting power to further the economic best interests of those who entrust their assets to portfolio managers and are the beneficial shareholders of public companies. If proxy advisory firms exceed that role—for example, by effectively exercising or being granted a measure of discretion over how shares are voted on specific proposals, or by failing to make proper disclosure regarding specific conflicts of interest afflicting a proxy advisory firm in connection with voting recommendations it is making—the proxy advisory firms so employed, and those engaging them, incur serious legal and regulatory consequences. The August 2019 Commission Guidance suggests that institutional investors should assess whether proxy advisory firms they hire have policies in place to identify, disclose, and address actual or potential conflicts of interest.

Portfolio manager discretion

Clarity is provided regarding the scope of portfolio managers' obligations to exercise a vote on proxy issues, and the obligations emphasize the broad discretion portfolio managers have—subject to appropriate procedures and safeguards—to refrain from voting on every, or even any, proposal put before shareholders for a vote.

Compliance

In light of the direction provided, proxy advisory firms and portfolio managers need to reassess their current practices and procedures and adopt appropriate changes necessitated by the Commission Guidance, while public companies should be aware of the direction provided to other stakeholders and consider it when developing policies and practices.



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