RK InvestLaw
A Public Benefit Corporation

February 3, 2020

Honorable Jay Clayton
Chairman
US Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

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

Dear Chairman Clayton:

For the reasons set forth below, the proposed amendments to the proxy rules relating to Proxy Voting Advice are beyond the power of the SEC. Further, they are unconstitutional because they would violate the First Amendment rights of shareholders to discuss the issues at stake in a proxy solicitation. We see nothing in the proposed rules or its supporting documents that would substantiate the strict scrutiny required for limits on protected speech.

In August 2019, the Commission expanded existing proxy rules by issuing an interpretive release, adopting a new definition of what constitutes a proxy solicitation.[1] The Commission announced that when shareholders hire proxy advisory services to provide information relating to items to be voted on at a company's annual meeting of shareholders, the advisory firm is itself engaging in a "proxy solicitation." That conclusion reverses years of interpretation and industry understanding, and conflicts with the regulatory purpose of the proxy rules themselves. It also conflicts with the longstanding rights of shareholders to seek advice from whatever service provider they choose, unfettered by government interference.[2]

The Commission has proposed to implement its novel definition by adopting rules that remove proxy advisory services from exemptions to which they are currently entitled, and that impose affirmative obligations on those service providers. The Commission asserts that these proposed changes are required because of a perceived risk of abuses.[3]

---

1 *See* Release No. 34-86721, Commission Interpretation and Guidance Regarding the Applicability of the Proxy Rules to Proxy Voting Advice, available at: https://www.sec.gov/rules/interp/2019/34-86721.pdf (effective September 10, 2019).

2 *See* Rule 14a-2(b)(3), 17 C.F.R. § 14a-2(b)(3).

See Release No. 34-87457, Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice (Nov. 5, 2019), available at: https://www.sec.gov/rules/proposed/2019/34-87457.pdf ("Proposed Amendments to Exemptions"). See p.11 ("[W]e are concerned about the risk of proxy voting advice businesses providing inaccurate or incomplete voting advice (including the failure to disclose material conflicts of interest) that could be relied upon to the detriment of investors.")

The expanded definition of who is deemed to be engaging in a proxy solicitation results in proxy advisory services becoming subject to SEC Rule 14a-9, the proxy antifraud rule. In that regard, an investment advisory service's proprietary advice to its clients based on public information provided in issuer documents would become subject to regulatory antifraud scrutiny and could be deemed by the Commission to be incomplete and thus materially misleading.

By taking these steps, the Commission is attempting to exercise regulatory authority over an aspect of business not expressly reserved to it by Congress. Not only would implementation impose substantial burdens on a service to shareholders already explicitly carved out from the current proxy rules, it interferes with a private business relationship.

As such, the very manner in which the proposed rules are designed to be implemented appears to violate the First Amendment. By expanding the definition of “solicit” or "solicitation" to include the analyses and recommendations provided by proxy advisory services to their clients, the Commission seeks to regulate private discourse between shareholders and the firms they hire to provide analyses based on criteria chosen by the shareholder. The result is to restrict contractual parties from having a free and frank interchange; in this case, that interchange relates to a shareholder's proxy voting choices. No statute grants the Commission that authority and - even if there were such a statute - the proposed rules would likely not withstand First Amendment scrutiny.

Advisory services analyze publicly-available information (which primarily comes from the issuer's own disclosure documents), synthesize it to meet specific client requests for information, and provide guidance on how that information relates to a client's stated investment objectives. Clients then incorporate that analysis into their own evaluation of how to vote on the issues presented at the shareholder meeting. This type of advice to clients is the essence of "viewpoint" speech.

As the Supreme Court explained in a recent ruling addressing the First Amendment, government “has no power to restrict expression because of its message, its ideas, its subject matter, or its content.” *Reed v. Town of Gilbert*, 576 U.S. _,135 S. Ct. 2218, 2226 (2015) (citation omitted). “[A] speech regulation targeted at specific subject matter is content based even if it does not discriminate among viewpoints within that subject matter.” *Id.* at 2230. On its face, the proposed Commission regulation seeks to limit discussions between a shareholder and its proxy advisory service where the subject matter is the question of how to vote proxies. The Commission does not otherwise attempt to limit the content of discussions about other topics for which the shareholder and its service provider may be engaged, such as potential compliance with ESG screens. Thus, the SEC's proposed regulation is aimed at the subject matter of the proxy advisory service. This is content regulation of speech at its most basic level.

Even if one were to accept the Commission's assertion that the integrity of research provided by proxy advisory services “could be” suspect,[4] what the government may not do is regulate the discussions between shareholders and their service providers. Just this past term, the Supreme Court explained that “viewpoint regulation” goes to the heart of First Amendment protections, striking down the Lanham Act limitation on registration of offensive trademarks: “The government may not discriminate against speech based on the ideas or opinions it conveys.” *Iancu v. Brunetti*, 588 U.S. _, 139 S. Ct. 2294, 2299 (2019).

When a publicly-traded company issues a statement about its financial affairs or solicits proxies, it generally publishes those statements first by filing them with the SEC - at which point they are deemed public - and then by making those statements widely available through a variety of channels. The information contained in the statement thus becomes part of the public discourse about the company.

When making statements to the public, publicly-traded companies are subject to strict government regulation, including the antifraud provisions relating to the statements made. *See, e.g.*, SEC Exchange Act Rules 10b-5, 13b2-2 and 14a-9.[5] However, once the company's statements become public, analysts and others are free to evaluate that information together with other publicly-available information and reach their own opinions and factual conclusions about what that information implies, whether good or bad. They also remain free to publicize those conclusions in the public domain or sell them to investment advisers or other interested persons, including voting shareholders.[6] These opinions and conclusions by analysts and proxy advisory firms are covered by the same heightened public discourse First Amendment protections as statements about public figures.[7]

Indeed, the Commission itself recognized these limitations in earlier public statements at the time it first wrote and revised its proxy solicitation rules. For example, the 1992 Commission, explaining its reluctance to regulate communications among shareholders, acknowledged that “[a] regulatory scheme that inserted the Commission staff and corporate management into every exchange and conversation among shareholders, their advisors and other parties on matters subject to a vote certainly would raise serious questions under the free speech clause of the First Amendment, particularly where no proxy authority is being solicited by such persons.”

---

4 Proposed Amendments to Exemptions at 39.

5 17 C.F.R. §§ 240.10b-5, 240.13b2-2 and 14a-9.

6 Depending on the forum in which those conclusions are published, they may subject the author to regulatory oversight.

7 *See New York Times v. Sullivan*, 376 U.S. 254 (1964) (proof of actual malice required in defamation action by public figure defendant). *See, e.g., Dun & Bradstreet, Inc. v. Greenmoss Builders, Inc.*, 472 U.S. 749 (1985) (extending *NY Times* to credit information reporter); *Bose v. Corp. v. Consumers Union of United States, Inc.*, 466 U.S. 485 (1984) (extending *NY Times* to reviewer of consumer product).

Regulation of Communications Among Shareholders, Release No. 34-31326 (Oct. 16, 1992) [57 Fed. Reg. 48276, 48279 (Oct. 22, 1992)].

But, more importantly, the Commission's recent effort to extend the definition of "proxy solicitation" beyond persons who are actually seeking to procure, withhold or revoke a proxy is an attempt by the Commission to expand its reach beyond any power Congress delegated to the agency.[8] While the Commission is given broad authority to regulate the solicitation of proxies as necessary and appropriate, that power is not unlimited. It may not redefine basic terms in the statute, nor may it seek to regulate an entire industry segment.

The Commission seeks to meet the issue of authority head on by asserting that the term "solicit" in the statute is ambiguous and did not have a sufficiently well-understood meaning when Congress enacted it in 1934. (*See* Proposed Amendments to Exemptions at 19 and note 48.) That argument seems forced. The term has a commonly-understood meaning, requires no definition as used in Section 14(a), and Congress accordingly did not provide one. It would be presumptuous of the Commission to assume that Congress erred in that respect.

The term "solicit" in Section 14(a)(1) is focused on the procurement of a proxy or consent by a registrant or other person seeking a proxy.[9] The term "solicit" therefore is aimed at the request for a proxy, not on the process by which the security holder makes a decision how or whether to give that proxy. The current proxy rule definition recognizes this ordinary meaning of "solicit." In Rule 14(a)(1)(*l*), the two subsections (i) and (ii) focus on the "request" for a proxy or execution of the proxy. The definition in subsection (iii), adopted in 1956, focuses on the "communications" designed to procure or revoke a proxy.[10] This latter definition cannot be divorced from the language of the statute, which is the process by which the registrant or other person seeks the proxy.

The Commission's recent interpretive guidance shifts this focus to how the security holder decides whether to give the proxy. This interpretation departs from its statutory antecedent. As explained by the Supreme Court in *J.I. Case Co. v. Borak*, 377 U.S. 426, 431 (1964), "[t]he purpose of §14(a) is to prevent management or others from obtaining authorization for corporate action by means of deceptive or inadequate disclosure in proxy solicitation." The focus of the statute is on the authorization for corporate action, not on the process of how security holders make decisions based on the solicitation materials. This same purpose was

---

8 The Commission enacted Rule 14a-1(*l*)(1)(iii) in its current form in 1956. That subsection specifies that a "solicitation" includes "[t]he furnishing of a form of proxy or other communication to security holders under circumstances reasonably calculated to result in the procurement, withholding or revocation of a proxy." 17 C.F.R. § 240.14a-1(*l*)(1)(iii).

9 The statute states: "to solicit . . . any proxy or consent or authorization in respect of any security (other than an exempted security) registered pursuant to section 12 of this title." 15 U.S.C. §78l(a)(1).

10 *See* 17 C.F.R. §240.14(a)(1)(*l*).

reiterated by the D.C. Circuit in *Business Roundtable v. SEC*, 905 F.2d 406 (D.C. Cir. 1990). There the court found, in rejecting a Commission rule to regulate share classes, that the proxy rules have a narrow focus rather than a broader general corporate suffrage mandate. "Proxy solicitations are, after all, only communications with potential absentee voters." *Id*. at 410. This purpose is best captured by the understanding that the proxy rules are aimed at the communications between persons actually requesting the votes of the security holders, not on the process security holders take in reaching that voting decision.

A unanimous Supreme Court recently reversed the Commission for engaging in a similar definitional sleight of hand. In *Digital Realty Trust, Inc. v. Somers*, 583 U.S. _, 138 S. Ct. 767 (2018), the Court struck down an SEC Rule that sought to define the term "whistleblower" contrary to the unambiguous statutory text. That same fate may well befall the Commission's current effort to redefine the term "solicit" in the proxy rules beyond its well-understood meaning. The Commission does not have the authority to extend the regulation beyond the commonly and long understood meaning of "solicit" as focused on those persons seeking to procure, withhold or revoke a proxy.

By expanding the definition of "solicit," the SEC seeks to regulate the content of the discussions between a shareholder and its proxy advisory service. This content-based regulation is contrary to modern First Amendment jurisprudence. For that reason, it is likely that a court would refrain from accepting the SEC's expanded definition when to do so would force the court: (i) to confront the First Amendment constitutional issue of whether Congress has the power to regulate the scope of private discourse among shareholders and their service providers; and, if so, (ii) to consider whether Congress has delegated that power to the SEC to implement by agency rulemaking.

There can be little question that the communication between the proxy advisory service and its client is speech. As stated by the Supreme Court, "the creation and dissemination of information are speech within the meaning of the First Amendment." *Sorrell v. IMS Health Inc.*, 564 U.S. 552, 570 (2011). What the Commission rules seek to do is regulate those communications by imposing advance burdens on the speaker regardless of the nature of the content of those communications. That is the essence of content or viewpoint regulation of speech barred by the First Amendment.

The analysis does not change if the proxy advisory service is offered by a registered investment adviser. The courts have long recognized the limits that the First Amendment places on the regulatory reach of the Investment Advisers Act of 1940 ("Advisers Act"). *See SEC v. Lowe*, 472 U.S. 181 (1985), and *SEC v. Wall Street Publishing, Inc.*, 851 F.3d 365 (D.C. Cir. 1988). The Advisers Act regulates the disclosure of conflicts of interest and fraudulent practices by an investment adviser, but it may not regulate the content of speech by the investment adviser to its client. In its interpretive release and related rule proposal, the Commission is going far beyond mandating disclosure of conflicts of interest or proscribing fraud. Instead, the Commission is improperly attempting to regulate the content of speech.

The Commission's attempt to overreach is not somehow "cured" because the securities laws apply to a highly-regulated industry. The First Amendment does not distinguish among types of businesses. Rather, the analysis of whether the Commission's proposed regulation violates the First Amendment is subject to "strict scrutiny," and requires that the agency's regulatory choices as to content regulation be the least intrusive of any alternative. *See Reed v. Town of Gilbert,* 135 S. Ct. at 2231-32. The Commission's proposed regulations do not appear to meet this test. Demanding disclosure of methodology and making proxy advisory firms give prior notice of the content of their advice is perhaps the *most* intrusive rather than the *least* intrusive alternative that could have been chosen by the Commission.

This First Amendment inquiry is fundamentally the same whether the question is analyzed under traditional First Amendment principles, or under the narrower commercial speech standard. “Commercial speech that is not false or deceptive and does not concern unlawful activities ... may be restricted only in the service of a substantial governmental interest, and only through means that directly advance that interest.” *Zauderer v. Office of Disc. Counsel*, 471 U.S. 626, 638 (1985). There is no factual basis for the notion that every communication between a proxy advisory firm and its client is potentially false or deceptive speech. At best the rule seeks to prevent possible incomplete communications between them, which is hardly a sound foundation for regulation of even commercial speech. The Commission rule proposal concludes there is a “risk” that there “could be” misleading conclusions communicated to security holders. The risk of possible misleading or incomplete communications is far below any First Amendment threshold for content regulation. Even if the record could establish a stronger case for potential deception, there are less intrusive means available to guard against potential false or deceptive disclosures.

Nor do the proposed rules advance a substantial governmental interest. As recognized in *Borak,* the governmental interest of Section 14(a) is on the full disclosure by the person seeking the proxy. Instead, the proposed rules interfere with communications between shareholders and their service providers.

The Commission has previously recognized the benefit of leaving those discussions unfettered by regulation: "The purpose of the proxy rules themselves are better served by promoting free discussion, debate and learning among shareholders and interested persons, than by placing restraints on that process to ensure that management has the ability to address every point raised in the exchange of views."[11] Its current releases offer no compelling argument as to why its earlier pronouncement is no longer valid.

That a shareholder seeks assistance in determining how a particular shareholder proposal in the already-filed proxy statement squares with the shareholder's individual investment policies and objectives is outside the scope of the Commission's regulatory reach. In the context of the First Amendment analysis, there is no legitimate government interest in requiring any sort of disclosure by the proxy advisory service of the content of its analysis.

---

[11] Regulation of Communications Among Shareholders, *Id.* at 48279.

The Commission is the watchdog for the investor - not for the publicly-traded company. The Commission should continue to respect its boundaries as it has in the past, and will hopefully, with the guidance of its staff and public input, set aside these proposals as beyond any legitimate governmental interest. We see no justification, let alone the strict scrutiny required under the First Amendment, for regulation of proxy advisory services.

Respectfully submitted,

/s/

Richard A. Kirby
Beth-ann Roth

R|K Invest Law, PBC