

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**INVESTMENT ADVISERS ACT OF 1940**  
**Release No. 3611 / May 23, 2013**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-15331**

**In the Matter of**

**INSTITUTIONAL  
SHAREHOLDER  
SERVICES INC.,**

**Respondent.**

**ORDER INSTITUTING ADMINISTRATIVE  
AND CEASE-AND-DESIST PROCEEDINGS  
PURSUANT TO SECTIONS 203(e) and  
203(k) OF THE INVESTMENT ADVISERS  
ACT OF 1940, MAKING FINDINGS, AND  
IMPOSING REMEDIAL SANCTIONS AND  
A CEASE-AND-DESIST ORDER**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against Institutional Shareholder Services Inc. (“ISS” or “Respondent”).

**II.**

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order (“Order”), as set forth below.

**III.**

On the basis of this Order and Respondent’s Offer, the Commission finds<sup>1</sup> that:

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<sup>1</sup> The findings herein are made pursuant to Respondent’s Offer and are not binding on any other person or entity in this or any other proceeding.

## **Summary**

1. From approximately 2007 through early 2012, an ISS employee (“the ISS Employee”) provided information to a proxy solicitor concerning how more than 100 of ISS’ institutional shareholder advisory clients (i.e., institutional investment managers) were voting their proxy ballots. In exchange for vote information, the proxy solicitor gave the ISS Employee meals, expensive tickets to concerts and sporting events, and an airline ticket. The ISS Employee, who had access to all of ISS’ clients’ proxy voting information, gathered the information by logging into ISS’ voting website from home or work and used his personal email account to communicate voting information to the proxy solicitor.

2. The ISS Employee’s breach was made possible in part by ISS’ failure to establish or enforce written policies and procedures reasonably designed, taking into consideration the nature of ISS’ business, to prevent the misuse of material, non-public information by ISS and its associated persons.

## **Respondent**

3. ISS (SEC File No. 801-55092), is a Delaware corporation with its principal place of business in Rockville, Maryland and has been registered with the Commission as an investment adviser since 1997. ISS is a wholly-owned subsidiary of MSCI Inc., a public company that provides indices and portfolio risk and performance analytics tools. In Part 2A of its Form ADV, ISS describes its advisory business as a “full-service proxy adviser... helping institutional investors make more informed proxy voting decisions, manage the complex process of voting their shares and report their votes to their stakeholders and regulators.” ISS has more than 1,700 clients to whom it provides several different services, including corporate governance research and vote recommendations and end-to-end proxy voting and distribution services.

## **Background**

4. Throughout the period of 2007 to early 2012 (“the relevant time period”), ISS provided an application via a confidential website to its institutional shareholder advisory clients to assist them in voting their proxy ballots. The current version of this application is called “ProxyExchange,” which ISS rolled out in early 2010, but prior versions of the application have existed throughout the relevant time period (2007 to early 2012). For shareholder meetings in the United States, ISS’ shareholder advisory clients used ProxyExchange (or its predecessor applications) to indicate their vote instructions after the ballots were received by ISS from third party proxy ballot providers through daily electronic feeds. After ISS’ clients indicated their vote instructions via ProxyExchange (or its predecessor applications), ISS then transmitted those instructions back to the appropriate ballot providers for delivery to the issuer. ISS clients had the ability to change their vote instructions at any time prior to the cutoff provided by the ballot provider, which typically in the United States is the day before the shareholder meeting. Employees of ISS’ account management group were responsible for assisting clients in their use of ProxyExchange for this purpose.

5. The client-specific vote information on ProxyExchange, including the number of shares a shareholder client had voted and the direction of the client’s vote, was confidential prior to the shareholder meeting. ISS’ shareholder advisory clients needed a user name and password to access ProxyExchange and vote their proxy ballots. Prior to a shareholder meeting, proxy

solicitors did not know for certain how a shareholder voted its proxy ballot unless the shareholder had disclosed the information.

6. ISS' clients also understood that, at least prior to a shareholder meeting, ISS would keep their vote information on ProxyExchange confidential. Some of ISS' shareholder advisory clients had detailed confidentiality provisions in their contracts. For example, one agreement between ISS and one of its shareholder advisory clients specifically required ISS to: only use the client's information as necessary to perform the services in the agreement, "safeguard, protect, and keep secret the Fund Information and to prevent its unauthorized, negligent or inadvertent use or disclosure," and not "disclose the Fund Information to any person or business entity other than a limited number of employees or officers of the Supplier on a need-to-know basis." In addition, several of ISS' clients did not share how they voted their proxy ballots with anyone prior to the shareholder meeting. It was also important to several of ISS' clients that ISS keep their vote information confidential, and some of these clients did not reveal their vote information before the shareholder meeting because, given the size of their positions, their vote could move the market price of the issuer's stock.

7. Within ISS, all employees in its account management group had access to a "View Only Ballot" section of ProxyExchange that provided those employees with read-only access to all of ISS' shareholder advisory clients' proxy voting information. Before ProxyExchange, this information was also available to ISS account managers, and, from approximately 2006 through 2009, the ISS Employee also had access to all of ISS' clients' voting information via a "Meeting Manager" database available to members of ISS' global proxy distribution group.

8. From 2007 through early 2012, the ISS Employee used "Meeting Manager" (from approximately 2007 through 2009) and ProxyExchange's "View Only Ballot" (from approximately 2010 to early 2012) to view client voting information and email it from his personal email account to a proxy solicitor. In a typical example, of which there are hundreds, the proxy solicitor would email the ISS Employee a list of ISS' clients with the name of an issuer and particular ballot propositions, and ask "how many & how voted." The ISS Employee would reply listing the number of shares voted by the shareholder and how the shareholder had voted. During the relevant time period, the ISS Employee emailed the proxy solicitor proxy voting information for more than 100 of ISS' institutional shareholder advisory clients.

9. The vote information the ISS Employee provided to the proxy solicitor related to a number of significant proxy contests that occurred during the relevant time period.

10. Throughout the relevant time period, the proxy solicitor firm purchased tickets and meals for the ISS Employee, who almost always used these tickets for himself and his friends or family, and did not sell the tickets. According to the proxy solicitor's expense reports, the proxy solicitor purchased approximately \$11,500 in sporting event and concert tickets for the ISS Employee. Except for one instance, no one from the proxy solicitor firm attended these events with the ISS Employee. The proxy solicitor also purchased sporting event tickets for at least two other ISS account managers, one of whom informed the proxy solicitor that two large shareholders had withheld their vote in a significant proxy contest.

11. In addition to tickets, the proxy solicitor sought reimbursement from the proxy solicitor firm for approximately \$20,000 in meals with the ISS Employee and his family, as well as meals with other ISS employees, from 2007 to 2011. According to ISS employees who attended the meals, there was never a business purpose for the meals and the fact that the proxy solicitor firm was entertaining ISS' account managers with meals was known to certain ISS managers, some of whom attended the meals.

12. Based on emails between the ISS Employee and the proxy solicitor, the ISS Employee provided the information to the proxy solicitor as a quid pro quo for the tickets and meals he received. When the ISS Employee replied to the proxy solicitor that he was swamped with work, the proxy solicitor would respond by offering tickets to a game. When the proxy solicitor needed to remind the ISS Employee to respond to one of his requests, he would sometimes write that he would try to get him tickets or take him to dinner. The ISS Employee would sometimes email the proxy solicitor requesting tickets to an event, and the proxy solicitor would respond with another request for more information. In one instance, the proxy solicitor asked for voting information and the ISS Employee responded that it would "cost you another game," and there were other times that the ISS Employee told the proxy solicitor that his requests for voting information would "cost" the proxy solicitor.

13. ISS had a Code of Ethics that prohibited unauthorized disclosures of confidential client information and barred employees from taking advantage of confidential client information for their personal benefit, but ISS did not establish, maintain or enforce sufficient policies or practices reasonably designed to prevent certain ISS account managers from sharing ISS' clients' confidential information in exchange for gifts.

14. ISS lacked sufficient controls over accountant managers' access to client vote information. As described above, when ISS rolled out ProxyExchange, ISS decided that all ISS account managers would have access to all of ISS' shareholder advisory clients' vote information via the "View Only Ballot" section. According to ISS, this was a business decision to enable account managers to have access to all shareholder advisory clients' vote information to allow an account manager to cover for another unavailable account manager in order to service a client.

15. When ISS rolled out ProxyExchange, the application could be audited to determine (i) when an employee accessed the application, (ii) what sections of the application the employee had accessed, (iii) whether the employee had made changes to any client voting data, and (iv) whether the employee had logged into the application from the employee's ISS computer or remotely from another computer. However, ISS did not review this data for the purpose of identifying potential employee misconduct. Had ISS done so, it could have identified that the ISS Employee frequently accessed the "View Only Ballot" section of the application remotely late at night or early in the morning from a remote location.

16. ISS lacked policies or procedures concerning the relationship between its account managers and proxy solicitors even though the potential misuse of material nonpublic information should have been clear to ISS' managers and compliance personnel. The supervisors of the ISS account managers who accepted meals or tickets from proxy solicitors were aware of the meals and events, and, in some cases, were invited to the meals and events.

Also, several supervisors at ISS attended meals paid for by proxy solicitors earlier in their careers when they were more junior employees. Similarly, account managers could recall communications among the employees, including managers, in the account management group when a proxy solicitor was being particularly aggressive in soliciting vote information. The proxy solicitor worked to cultivate relationships with employees in ISS' account management group, but ISS did not provide training for its account managers concerning how to interact appropriately with a proxy solicitor even though: (a) one of the most important roles of a proxy solicitor is to inform their clients how shareholders are voting their proxies, (b) during the relevant time period, there was virtually no legitimate business reason for ISS' account managers to have relationships with proxy solicitors, and (c) all of ISS' account managers had access to voting information that would be very helpful to proxy solicitors.

17. MSCI, ISS' parent company, had a written policy that prohibited ISS employees from receiving gifts unless of a nominal value, or business entertainment unless reasonable and appropriate, but many ISS account managers were unclear on how to interpret the policy and when it applied. ISS failed to provide adequate training for its employees regarding application of the gift policy, and despite being generally aware of certain meals and events, ISS managers never took steps to determine whether the meals were reasonable and appropriate under the policy. The gifts policy invited employees to contact a legal or compliance person if they had questions about the policy, but the policy did not require employees to report gifts.

18. In addition to the proxy solicitor firm that exchanged meals and tickets with the ISS Employee for vote information, several ISS account managers were treated to meals and/or sporting event tickets by other proxy solicitor firms. One proxy solicitor developed a friendship with an ISS account manager and treated him to meals on at least two occasions. After receiving the meals, the ISS account manager told the proxy solicitor in approximately 2009 how specific ISS clients were voting in a proxy contest.

19. Finally, even though many ISS account managers worked in offices where there were no ISS compliance personnel, ISS did not routinely review its employees' emails unless there was suspicion of wrongdoing. Although the ISS Employee communicated with the proxy solicitor from his personal account, other ISS employees planned their outings with the proxy solicitor using their ISS email accounts. Also, at least one ISS employee used his ISS email account to email confidential client information (whether, but not how, specific ISS shareholder advisory clients had voted their proxies) to a proxy solicitor.

20. As a result of the conduct described above, ISS willfully<sup>2</sup> violated Section 204A of the Advisers Act. Section 204A requires advisers to "establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of such advisers business, to prevent the misuse" in violation of the Advisers Act or the Securities Exchange Act of 1934 ("Exchange Act") "of material, nonpublic information" by the adviser or any person associated with the adviser. In this case, ISS violated Section 204A because it failed to establish

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<sup>2</sup> A willful violation of the securities laws means merely "that the person charged with the duty knows what he is doing." *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting *Hughes v. SEC*, 174 F.2d 969, 977 (D.C. Cir. 1949)). There is no requirement that the actor "also be aware that he is violating one of the Rules or Acts." *Id.* (quoting *Gearhart & Otis, Inc. v. SEC*, 348 F.2d 798, 803 (D.C. Cir. 1965)).

and enforce policies and procedures reasonably designed to prevent the misuse of ISS' shareholder advisory clients' material, nonpublic proxy voting information.

### **Respondent's Cooperation and Remedial Acts**

21. In determining to accept ISS' settlement offer, the Commission considered remedial acts promptly undertaken by Respondent and cooperation afforded the Commission staff. In particular, after the conduct of the ISS Employee was identified but prior to resolution of this proceeding ISS, among other things, (i) implemented a Policy on Interactions and Communications with Proxy Solicitors and other Advisory Firms; (ii) conducted training of its employees regarding the new policy and additional training on its code of ethics and gifts and entertainment policy; (iii) implemented modifications to reduce access to and enhance the monitoring capabilities of ProxyExchange; and (iv) is instituting a gift log requiring employees to report on gifts received.

### **Undertakings**

22. ISS undertakes to:

A. Retain, at its expense and within thirty (30) days of the issuance of this Order, an independent consultant (the "Consultant") not unacceptable to the staff of the Division of Enforcement ("Commission Staff"). Respondent shall require the Consultant to conduct a comprehensive review of ISS's supervisory and compliance policies and procedures reasonably designed to ensure that its proxy voting services business complies with the Advisers Act in connection with the treatment of confidential information, communications with proxy solicitors, and gifts and entertainment.

B. Require the Consultant to complete its review and submit a written report (the "Report") to ISS and Commission staff within one hundred twenty (120) days of the issuance of this Order. ISS shall require that the Report describe the review performed, the conclusions reached, and recommendations for any changes in or improvements to ISS's supervisory and compliance policies and procedures.

C. Within sixty (60) days of receiving the Report, adopt and implement all recommendations contained in the Report; provided, however, that as to any recommendation that ISS considers to be, in whole or in part, unduly burdensome or impractical, ISS may submit in writing to the Consultant, within thirty (30) days of receiving the Report, an alternative policy, practice, or procedure designed to achieve the same objective or purpose. Within forty-five (45) days of receiving the Report, ISS and the Consultant shall attempt in good faith to reach an agreement relating to each recommendation that ISS considers to be unduly burdensome or impractical. ISS shall ultimately abide by the determinations of the Consultant.

D. Require the Consultant to enter into an agreement that provides that for the period of engagement and for a period of two years from completion of the engagement, the Consultant shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with ISS, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity. The agreement will also provide that the Consultant will require that any firm with which the Consultant is affiliated or of which the Consultant is a member, and

any person engaged to assist the Consultant in performance of the Consultant's duties under this Order shall not, without prior written consent of Commission staff, enter into any employment, consultant, attorney-client, auditing or other professional relationship with ISS, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such for the period of the engagement and for a period of two years after the engagement.

E. To ensure the independence of the Consultant, ISS shall not have the authority to terminate the Consultant without prior written approval of Commission staff and shall compensate the Consultant and persons engaged to assist the Consultant for services rendered pursuant to this Order at their reasonable and customary rates.

F. For good cause shown, the Commission's staff may extend any of the procedural dates relating to the undertakings. Deadlines for procedural dates shall be counted in calendar days, except that if the last day falls on a weekend or federal holiday, the next business day shall be considered to be the last day.

23. Within thirty (30) days of the issuance of this Order, ISS undertakes to post a copy of or a link to this Order on the homepage of ISS' website and to maintain the copy or link for a period of six (6) months.

24. ISS shall certify, in writing, compliance with the undertakings set forth above. The certification shall identify the undertaking, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission's staff may make reasonable requests for further evidence of compliance, and ISS agrees to provide such evidence. The certification and supporting material shall be submitted to Kevin M. Kelcourse, Assistant Director, Asset Management Unit, Boston Regional Office, Securities and Exchange Commission, 33 Arch Street, Suite 2300, Boston, MA 02110, with a copy to the Office of the Chief Counsel of the Enforcement Division (Securities and Exchange Commission, 100 F Street, NE, Washington, DC, 20549), no later than sixty (60) days from the date of completion of the undertaking.

#### **IV.**

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent's Offer.

Accordingly, pursuant to Sections 203(e) and 203(k) of the Advisers Act, it is hereby ORDERED that:

A. Respondent ISS cease and desist from committing or causing any violations and any future violations of Section 204A of the Advisers Act.

B. Respondent ISS is censured.

C. Respondent ISS shall, within 10 days of the entry of this Order, pay a civil money

penalty in the amount of \$300,000 to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. Payment must be made in one of the following ways:

- (1) Respondent ISS may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- (2) Respondent ISS may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or
- (3) Respondent ISS may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center  
Accounts Receivable Branch  
HQ Bldg., Room 181, AMZ-341  
6500 South MacArthur Boulevard  
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying ISS as the Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Kevin M. Kelcourse, Assistant Director, Asset Management Unit, Boston Regional Office, Securities and Exchange Commission, 33 Arch Street, Suite 2300, Boston, MA 02110. If transmitting payment electronically by wire or directing payment from a bank account via Pay.gov, Respondent shall send a letter to Mr. Kelcourse confirming the date of payment, method of payment (e.g., wire or Pay.gov), and tracking information (e.g., agency tracking identification number).

D. Respondent ISS shall comply with the undertakings enumerated in Section III above.

By the Commission.

Elizabeth M. Murphy  
Secretary