



National Investor Relations Institute

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August 3, 2017

The Honorable Jay Clayton  
Chairman  
Securities and Exchange Commission  
100 F Street, NE  
Washington, D.C. 20549

Subject: Proxy Advisory Firms – Shareholder Voting Practices

Dear Chairman Clayton:

On behalf of the National Investor Relations Institute<sup>1</sup> (“NIRI”), I am writing to bring to the attention of the Securities and Exchange Commission several shareholder voting practices being used by the two largest proxy advisory firms, Institutional Shareholder Services (“ISS”), and Glass Lewis (“Glass Lewis”).

NIRI believes that these shareholder voting practices may be inconsistent with Rule 14a-2(b)(1) under the Securities Exchange Act of 1934 (“Exchange Act”) and the guidance provided in SEC Staff Legal Bulletin 20.<sup>2</sup> These practices also do not appear to be compliant with SEC requirements under the Investment Advisers Act of 1940 (“Investment Advisers Act”).

What follows are descriptions of the ISS and Glass Lewis automated shareholder voting systems and the practices that NIRI believes may be non-compliant.

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<sup>1</sup> Founded in 1969, the National Investor Relations Institute (“NIRI”) is the professional association of corporate officers and investor relations consultants responsible for communication among corporate management, shareholders, securities analysts, and other financial community constituents. NIRI is the largest professional investor relations association in the world, with more than 3,300 members representing over 1,600 publicly held companies and \$9 trillion in stock market capitalization.

<sup>2</sup> Exchange Act Rule 14a-2(b)(1) is codified at 17 C.F.R. § 240.14a-2(b)(1). *See also* Proxy Voting: Proxy Voting Responsibilities of Investment Advisers and Availability of Exemptions from the Proxy Rules for Proxy Advisory Firms, Staff Legal Bulletin No. 20, June 30, 2014 (hereinafter “Staff Legal Bulletin 20”).

The ISS Proxy Exchange Voting System

ISS offers a shareholder voting service that enables its clients to transmit voting instructions electronically to the various intermediaries involved in tabulating shares at shareholder meetings. Recent court filings in an appraisal lawsuit in Delaware against Dell, Inc. describe in detailed fashion the inner workings of the ISS Proxy Exchange (“ISS PX”) voting system.<sup>3</sup>

For all proxy voting participants, the process starts with proxy materials being sent to ISS electronically from Broadridge Financial Solutions, Inc. (“Broadridge”), on behalf of each institutional client using ISS’s shareholder voting services.<sup>4</sup>

After receiving these proxy materials, ISS then creates a “Meeting Record” for each client, which generates an electronic ballot to be used by ISS to transmit the voting instructions for each client to the entities involved in tabulating shares at each shareholder meeting.<sup>5</sup> After a Meeting Record is established, an informational email is typically sent to each ISS client, permitting the client to access its Meeting Record for a specific shareholder meeting.<sup>6</sup>

Each ISS client establishes general voting guidelines and policies in advance of voting on actual proposals and matters at a shareholder meeting. When a Meeting Record is established, ISS permits the Meeting Record to be automatically pre-populated with voting instructions for each matter on the proxy card, using the ISS client’s general guidelines and policies as the default positions.<sup>7</sup>

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<sup>3</sup> See Certain Petitioners’ Brief in Support of Motion for Summary Judgment Regarding Entitlement to Appraisal, and in Opposition to Respondent’s Motion for Summary Judgment, *In Re Appraisal of Dell Inc.*, Del. Ch., Consol. C. A. No. 9322, January 8, 2016, available at [http://www.shareholderforum.com/dell/Library/20160108\\_DelCh-Petitioners-brief.pdf](http://www.shareholderforum.com/dell/Library/20160108_DelCh-Petitioners-brief.pdf) (hereinafter “T. Rowe Price Brief”); and Respondent Dell Inc.’s Reply Brief in Support of Motion for Partial Summary Judgment, and Opposing Petitioners’ Cross-Motion, as to Petitioners Who Voted in Favor of the Merger, *In re Appraisal of Dell Inc.*, Del. Ch., Consol. C. A. No. 9322, February 15, 2016, available at [http://www.shareholderforum.com/dell/Library/20160208-0215\\_DelCh-Respondent-brief.pdf](http://www.shareholderforum.com/dell/Library/20160208-0215_DelCh-Respondent-brief.pdf). NIRI does not have a position regarding the Dell appraisal case. The facts presented in this letter are only used for the purpose of illustrating how the ISS Proxy Exchange voting system operates in practice.

<sup>4</sup> *T. Rowe Price Brief* at 18. After proxy materials are distributed to beneficial owners in the street name system, voting instructions from these owners are typically submitted to Broadridge Financial Solutions, Inc. (“Broadridge”), as an agent of the broker-dealers and banks holding corporate shares in nominee name. Broadridge then submits aggregated voting instructions for all of its nominee clients to the tabulator for each shareholder meeting.

<sup>5</sup> *Id.* at 18-19.

<sup>6</sup> *Id.* at 19.

<sup>7</sup> *Id.* See also *In Re: Appraisal of Dell Inc.*, Consol. C.A. No. 9322-VCL, at 9-10 (Del. Ch. May 11, 2016), available at [http://www.shareholderforum.com/dell/Library/20160511\\_DelCh-Opinion.pdf](http://www.shareholderforum.com/dell/Library/20160511_DelCh-Opinion.pdf) (“The T. Rowe Voting System would pre-populate the [ISS] meeting record with voting instructions that matched T. Rowe’s standard voting policies.”).

In the event that an ISS client seeks to deviate from its standard voting guidelines or policies, it is allowed to manually enter a voting decision modification into its interface with the ISS PX system.<sup>8</sup> However, if no affirmative action is taken by a client, the ballot for each shareholder meeting is automatically submitted for tabulation, using the default voting instructions.

### The Glass Lewis Viewpoint Voting System

Based on public documentation, it appears that the Glass Lewis voting system—called Viewpoint—operates in a similar manner. Glass Lewis clients develop custom voting guidelines and then the staff of Glass Lewis applies these policies to generate recommended voting decisions for each shareholder ballot. This process is described in the most recent Glass Lewis Best Practices Principles paper:

All clients ... receive the same Glass Lewis Proxy Paper report, in the same format, at the same time and with the same recommendations. ... In conjunction with the publication of the Proxy Paper report, Glass Lewis also generates and displays client custom recommendations through its Web-based voting platform, Viewpoint.

Viewpoint applies client custom policies to each [shareholder] meeting using a proprietary rules engine developed by Glass Lewis. The logic-based rules engine technology and agnostic data collection process used by Glass Lewis ensure that custom policies are applied in an objective and consistent manner that is fully logged and auditable. As upcoming meetings are identified, each proposal is categorized by Glass Lewis research analysts. The rules engine then references the relevant client policies for those proposals, determines the data points that are required to apply the policies, and prompts the research analysts working on that meeting to furnish the data points. Once all of the necessary information has been gathered and reviewed for accuracy, the rules engine processes the relevant rules and generates the custom recommendations for clients.<sup>9</sup>

The Glass Lewis Viewpoint system generates an electronic ballot for each shareholder meeting that contains each client's custom voting recommendations based on its pre-established governance policies. This ballot is then voted automatically at the appropriate shareholder meeting unless a client decides to manually override the default recommendations:

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<sup>8</sup> *T. Rowe Price Brief* at 19.

<sup>9</sup> Glass Lewis, "Best Practice Principles for Providers of Shareholder Voting Research & Analysis, Statement of Compliance for the Period of 1 January 2016 Through 31 December 2016" at 10, March 2017, *available at* <http://www.glasslewis.com/wp-content/uploads/2017/03/GL-Compliance-Statement-2017.pdf>.

Whether clients elect to vote according to a custom policy, a hybrid policy or the Glass Lewis house policy, they control when and how votes are cast. Viewpoint provides clients with the ability to override recommendations triggered by their selected policy or policies, which they often elect to do. Clients are responsible for designing and managing their vote management preferences, assigning review and voting rights to users, etc. Glass Lewis is responsible for ensuring that voting is conducted in accordance with client instructions.<sup>10</sup>

Based on this explanation, it is NIRI's understanding that a Glass Lewis client seeking to deviate from its standard voting guidelines or policies is allowed to manually enter a voting decision modification into its interface with the Viewpoint system.<sup>11</sup> However, NIRI also understands that if no affirmative action is taken by a client, the ballot for each shareholder meeting is automatically submitted for tabulation, using the default voting instructions.

Proxy Advisory Firm Compliance with SEC Staff Legal Bulletin 20

NIRI believes that these ISS and Glass Lewis shareholder voting services may be operating in a manner that is inconsistent with Question 7 of SEC Staff Legal Bulletin 20, which interprets the exemption to the proxy solicitation rules provided by Exchange Act Rule 14a-2(b)(1).

Staff Legal Bulletin 20 was issued by the SEC Divisions of Investment Management and Corporation Finance on June 30, 2014.<sup>12</sup> Question 7 of the guidance addresses the circumstances in which the proxy solicitation exemption under Exchange Act Rule 14a-2(b)(1) may not apply to a proxy advisory firm offering a certain type of shareholder voting service:

**Question 7.** Where a shareholder (such as an institutional investor) retains a proxy advisory firm to assist in the establishment of general proxy voting guidelines and policies and authorizes the proxy advisory firm to execute a proxy or submit voting instructions on its behalf, and permits the proxy advisory firm to use its discretion to apply the guidelines to determine how to vote on particular proposals, may the proxy advisory firm providing such services rely on the exemption from the proxy rules in Exchange Act Rule 14a-2(b)(1)?

**Answer.** No. Rule 14a-2(b)(1) provides an exemption from most provisions of the federal proxy rules for 'any solicitation by or on behalf of

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<sup>10</sup> *Id.* at 11.

<sup>11</sup> *Id.*

<sup>12</sup> *Staff Legal Bulletin 20, supra* note 2.

any person who does not, at any time during such solicitation, seek directly or indirectly, either on its own or another's behalf, the power to act as a proxy for a security holder and does not furnish or otherwise request, or act on behalf of a person who furnishes or requests, a form of revocation, abstention, consent or authorization.' *The exemption would not be available for a proxy advisory firm offering a service that allows the client to establish, in advance of receiving proxy materials for a particular shareholder meeting, general guidelines or policies that the proxy advisory firm will apply to vote on behalf of the client.*

In this instance, the proxy advisory firm would be viewed as having solicited the 'power to act as a proxy' for its client. This would be the case even if the authority was revocable by the client.<sup>13</sup> (emphasis added).

Based on the public documentation presented in this letter, NIRI believes that the Proxy Exchange and Viewpoint shareholder voting systems may not be in compliance with the guidance in Staff Legal Bulletin 20 and, therefore, these voting services should not be eligible for the proxy solicitation exemption under Exchange Act Rule 14a-2(b)(1).

ISS and Glass Lewis clients establish their general voting guidelines and policies in advance of each year's proxy season. These clients authorize ISS and Glass Lewis to apply their general or custom guidelines and policies to the proposals at each shareholder meeting, for the purpose of developing default voting decisions. The ISS and Glass Lewis voting systems then electronically generate a ballot that contains voting instructions that represent these default positions, based on each client's general guidelines and policies.

While a client is permitted to override these pre-programmed voting instructions, the client does not need to take any action whatsoever to confirm, approve, or submit these votes for tabulation. ISS and Glass Lewis will automatically submit these votes on the client's behalf, whether or not the client has reviewed, changed, or approved the voting decisions made by ISS and Glass Lewis.<sup>14</sup>

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<sup>13</sup> *Id.*

<sup>14</sup> Similar concerns were expressed recently by a corporate attorney in a Harvard Law School blog post. See Thomas J. Dougherty, Skadden, Arps, Slate, Meagher & Flom LLP, "'Pre-Populated' Proxy Protocols and the Narrowing of Proxy Participation," Harvard Law School Forum on Corporate Governance and Financial Regulation, July 20, 2017, available at <https://corpgov.law.harvard.edu/2017/07/20/pre-populated-proxy-protocols-and-the-narrowing-of-proxy-participation/> (hereinafter "Dougherty Article") ("In practice, under this 'pre-populated' voting instruction protocol, an institutional investor can specify its presumptive votes on proxy issues (even a merger vote) without reference to the particular proxy disclosures and nuances of particular issuer specifics. ... This process is dark. There is no regulation or transparency. It is worth corporate directors' and SEC attention.") (emphasis in original).

We do not believe that Staff Legal Bulletin 20 intended to extend the exemption in these circumstances. The ISS and Glass Lewis voting systems use pre-established guidelines and policies to generate default voting instructions for each client's electronic ballot and then the system submits these votes on behalf of each client, without any requirement that the client take any type of affirmative action. If ISS and Glass Lewis are permitted to automatically submit votes for pre-established default positions without any subsequent action or voting decisions by a client, then these proxy advisory firms have successfully solicited the "power to act as a proxy" for each of their clients that use these voting systems.

#### The Investment Advisers Act

The automatic submission of voting instructions by ISS and Glass Lewis without any affirmative action by their clients also appears to be inconsistent with the fiduciary responsibilities of investment advisers under the Investment Advisers Act.

The ISS and Glass Lewis voting systems are almost completely automated. The proxy materials for street name shares are sent electronically by Broadridge directly to these proxy advisory firms. These firms apply a client's pre-established guidelines and policies to each proposal at a shareholder meeting and pre-populate default voting instructions into an electronic ballot. Before the shareholder meeting, each client's shares are voted as the system has mechanically instructed, without an investment adviser even having to press a "Submit" button. Everything is done without human interface and an adviser only needs to interact with the ISS or Glass Lewis voting system if it wants to change a vote from its general guidelines and policies, or if it disagrees with an ISS or Glass Lewis voting recommendation.<sup>15</sup>

These highly automated voting systems do not appear to be compliant with the SEC's Proxy Voting Rule, in which each investment adviser is required to "vote proxies in the best interest of its clients."<sup>16</sup> An entirely mechanical system that votes shares without any required interaction on the part of the investment adviser at the time of proxy voting also appears to be

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<sup>15</sup> NIRI also believes that this type of automated voting system is inconsistent with Question 5 of Staff Legal Bulletin No. 20. If the primary responsibility of an investment adviser is only to develop general guidelines and policies for proxy voting, with Proxy Exchange or Viewpoint handling all other functions, then it is doubtful that ISS and Glass Lewis clients are properly ascertaining whether either proxy advisory firm has the "capacity and competency to adequately analyze proxy issues, which includes the ability to make voting recommendations based on materially accurate information." *Staff Legal Bulletin 20* at Question 5. Investment advisers that are relying solely on this type of automated voting system do not appear to be complying with this guidance.

<sup>16</sup> See *Staff Legal Bulletin 20* at Question 1, citing Rule 206(4)-6 under the Investment Advisers Act. In NIRI's opinion, it is hard to argue that a fiduciary has cast proxy votes in the best interest of its clients if no person within the fiduciary's firm has even read the applicable proxy statement. See *Dougherty Article* ("[I]nstitutions increasingly have added the practice of 'pre-population' of proxy votes by which the vendor suggests or predicts, in their view, how an institution would *likely* vote based on an institution's general policies. The institution is then free to leave in place the vendor's suggested pre-populated vote, or negate it. But the latter requires timely institutional initiative in order that it matter. ... [W]ith 'pre-population' it is entirely possible that the institution itself has *no one* who actually read the issuer's proxy statement.") (emphasis in original).



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inconsistent with the SEC requirement that each adviser develop and implement written policies and procedures that are reasonably designed to ensure that proxies are voted in the best interests of its clients.<sup>17</sup>

#### Conclusion

NIRI urges the SEC to evaluate the ISS and Glass Lewis shareholder voting systems and to consider appropriate actions to require these proxy advisory firms to operate their voting systems in a manner that is compliant with Exchange Act Rule 14a-2(b)(1), Staff Legal Bulletin 20, and SEC requirements under the Investment Advisers Act.

Please feel free to contact us at NIRI if you need additional information or are interested in discussing these issues further. Thank you for your consideration of our views on this matter.

Sincerely,

A handwritten signature in black ink, reading "Gary A. LaBranche". The signature is fluid and cursive, with a small mark at the end.

Gary A. LaBranche, FASAE, CAE  
President and CEO  
National Investor Relations Institute

cc: The Honorable Kara M. Stein  
The Honorable Michael S. Piwowar  
William Hinman, Director, Division of Corporation Finance  
David Grim, Director, Division of Investment Management

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<sup>17</sup> See *Id.* at Answer to Question 1, citing Rule 206(4)-7 under the Investment Advisers Act.