

December 31, 2018

*Via Electronic Filing*

Mr. Brent J. Fields  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

**Re: SEC Staff Roundtable on the Proxy Process (File No. 4-725)**

Dear Mr. Fields:

The Investment Adviser Association<sup>1</sup> (**IAA**) appreciates the opportunity to comment on the recent SEC Staff Roundtable on the Proxy Process (**Roundtable**). We commend the Staff for inviting a well-balanced selection of speakers to the Roundtable who provided a variety of perspectives on important proxy issues. The Roundtable confirmed what has been evident for some time, and around which there is consensus – that the proxy infrastructure is broken and in need of urgent attention. It underscored the need to address issues relating to proxy voting mechanics and technology, including, for example, end-to-end vote confirmation and verification. Certainly, our members want assurances that the proxy votes that they cast on behalf of their clients are in fact counted and are counted accurately. Investors and those voting on behalf of investors should be able to rely on the integrity of the proxy process.

The Roundtable also addressed the politically heated, but far less systemically important, topic of proxy advisory firms.<sup>2</sup> Focusing on proxy advisory firms is a potential distraction from the pressing proxy infrastructure weaknesses highlighted at the Roundtable, and we submit that the Commission should tackle infrastructure first and foremost. However, it is clear to us that the services of proxy advisory firms are facing significant challenges from the issuer community and others and therefore this letter describes and explains the importance of the use of such firms by SEC-registered investment advisers.<sup>3</sup>

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<sup>1</sup> The IAA is a not-for-profit association dedicated to advancing the interests of SEC-registered investment advisers. The IAA's more than 650 member firms manage more than \$25 trillion in assets for a wide variety of individual and institutional clients, including pension plans, trusts, mutual funds, private funds, endowments, foundations, and corporations. For more information please visit our website: [www.investmentadviser.org](http://www.investmentadviser.org).

<sup>2</sup> The third topic addressed at the Roundtable was shareholder proposals. We do not discuss that topic in this letter.

<sup>3</sup> The IAA has a longstanding interest in preserving the ability of investment advisers to access the services of proxy advisory firms. Indeed, IAA President and CEO Karen Barr participated in a 2013 SEC roundtable on this issue. See Proxy Advisory Services Roundtable website at <https://www.sec.gov/spotlight/proxy-advisory-services.shtml>.

Investment advisers routinely vote proxies on behalf of and in the best interest of their clients. In so doing, they retain the services of proxy advisory firms, which provide important support, particularly voting-related administration services. Indeed, investment advisers of all sizes would face extreme logistical difficulty if they were unable to use these services to assist in the mechanics of voting proxies and for research. We strongly object to efforts to restrict advisers' use of these firms and to regulation that would make these firms' services more expensive for advisers and their clients and increase barriers to entry.

We discuss below:

- Advisers' use of proxy advisory firms for a range of administrative and research services;
- Advisers' understanding of their obligation to vote proxies in the best interest of their clients; and
- The likelihood that additional regulation of proxy advisory firms would increase the cost of their services for advisers and their clients, or increase barriers to entry, without commensurate benefits.

We also address the suggestions of some commentators that the votes of portfolio companies held by investment companies (**funds**) be "passed through" to fund shareholders or that funds solicit the views of fund shareholders on such proxy votes. As discussed below, these suggestions would be neither appropriate nor workable and we would oppose them.

#### **I. Advisers Use Proxy Advisory Firms for a Range of Administrative and Research Services**

As several panelists discussed at the Roundtable, investment advisers use proxy advisory firms for a number of significant administrative services, such as voting mechanics, data tracking and aggregation, and workflow management. These administrative services are critically important for advisers that manage hundreds, if not thousands, of proxy votes each year.

Certain investment advisers provide their own proxy voting guidelines to proxy advisory firms, and those firms customize their recommendations to the advisers' guidelines and execute the proxy votes. Other advisers receive research and recommendations from proxy advisory firms. Advisers may choose to receive information based on standard benchmark policies or more specific policies, such as socially responsible investing. For these advisers, the research and recommendations provided by the proxy advisory firms are inputs they use to make their own independent decisions on how to vote proxies consistent with their own policies and client guidelines. For proxy issues that are routine and not contested, it should not be surprising that most shareholders vote consistently with one another and with recommendations of proxy advisory firms and, indeed, with management. On non-routine or contested issues, however, such as shareholder proposals, including those related to compensation, evidence shows that there is

diversity among shareholder votes.<sup>4</sup> As discussed at the Roundtable, it is therefore not accurate to characterize investment advisers as “robo voting” in lockstep with the recommendations of proxy advisory firms.

## **II. Advisers Understand Their Obligation to Vote Proxies in the Best Interest of Their Clients**

Investment advisers are currently subject to substantial regulation in their voting of proxies on behalf of their clients. The Investment Advisers Act of 1940 (**Advisers Act**) “establishes a federal fiduciary standard for investment advisers,” which “comprises a duty of care and a duty of loyalty.”<sup>5</sup> In addition, in 2003, the Commission adopted Rule 206(4)-6 under the Advisers Act (the **Proxy Voting Rule**) which is specifically “designed to ensure that advisers vote proxies in the best interest of their clients and provide clients with information about how their proxies are voted.”<sup>6</sup> In adopting the rule, the Commission stated that “[t]he duty of care requires an adviser with proxy voting authority to monitor corporate events and to vote proxies. To satisfy its duty of loyalty, the adviser must cast the proxy votes in a manner consistent with the best interest of its client and must not subrogate client interests to its own.”<sup>7</sup>

Under the Proxy Voting Rule, advisers are required to adopt and implement written policies and procedures that are reasonably designed to ensure that each adviser votes client securities in the client’s best interest.<sup>8</sup> These policies and procedures must address material conflicts that may arise between an adviser and its clients. Advisers must describe these policies and procedures to their clients and provide them to requesting clients. Advisers must also disclose to clients how they may obtain information about how the adviser voted client proxies. The adviser’s proxy voting policies and procedures are part of the compliance program advisers

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<sup>4</sup> See *Funds and Proxy Voting: Funds Vote Thoughtfully and Independently*, Investment Company Institute (Nov. 7, 2018), available at [https://www.ici.org/viewpoints/view\\_18\\_proxy\\_voting\\_results](https://www.ici.org/viewpoints/view_18_proxy_voting_results).

<sup>5</sup> *Proposed Commission Interpretation Regarding Standard of Conduct for Investment Advisers; Request for Comment on Enhancing Investment Adviser Regulation*; SEC Rel. IA-4889 (Apr. 18, 2018), 83 Fed. Reg. 21203, 21205 (May 9, 2018), available at <https://www.federalregister.gov/documents/2018/05/09/2018-08679/proposed-commission-interpretation-regarding-standard-of-conduct-for-investment-advisers-request-for> (reference omitted).

<sup>6</sup> *Proxy Voting by Investment Advisers*, SEC Rel. IA-2106 (Jan. 31, 2003), 68 Fed. Reg. 6585 (Feb. 7, 2003), available at <https://www.gpo.gov/fdsys/pkg/FR-2003-02-07/pdf/03-2952.pdf>.

<sup>7</sup> *Id.* at 6586.

<sup>8</sup> Voting proxies in a client’s best interest is not inconsistent with an adviser applying its proxy voting policies consistently across issuers, particularly on uncontested and routine matters. In fact, when it adopted Rule 206(4)-6, the Commission stated that, in order to show that proxy votes are voted in a client’s best interest and are not affected by an adviser’s conflicts of interest, an adviser may vote “based on a pre-determined voting policy.” *Id.* at 6588. The Commission also made clear, and we agree, that Rule 206(4)-6 benefits clients “by allowing them to understand how their advisers vote proxies.” *Id.* at 6589.

must implement, and advisers must review their adequacy at least annually, as required by Rule 206(4)-7 under the Advisers Act (the **Compliance Program Rule**).<sup>9</sup>

The Division of Investment Management provided guidance to investment advisers regarding their responsibilities “in voting client proxies and retaining proxy advisory firms” in Staff Legal Bulletin No. 20, published in 2014 (**Bulletin**).<sup>10</sup> The Bulletin addresses a number of issues, including steps advisers could take to show that proxy votes are cast consistently with their clients’ best interest and the advisers’ proxy voting procedures, the fact that advisers and clients may agree that not all proxies must be voted, considerations advisers may wish to take in retaining proxy advisory firms, and oversight of proxy advisory firms.

Regarding due diligence and oversight of proxy advisory firms, the Bulletin outlines issues for investment advisers to consider when evaluating whether to retain or continue retaining a proxy advisory firm to provide proxy voting recommendations. These include the “adequacy and quality of the proxy advisory firm’s staffing and personnel,” the “robustness” of the proxy advisory firm’s policies and procedures “regarding its ability to (i) ensure that its proxy voting recommendations are based on current and accurate information and (ii) identify and address any conflicts of interest and any other considerations that the investment adviser believes would be appropriate in considering the nature and quality of the services provided by the proxy advisory firm.”<sup>11</sup> The Bulletin goes on to explain that advisers should “adopt and implement policies and procedures that are reasonably designed to provide sufficient ongoing oversight of the third party in order to ensure that the investment adviser, acting through the third party, continues to vote proxies in the best interests of its clients.”<sup>12</sup> Advisers also “should establish and implement measures reasonably designed to identify and address the proxy advisory firm’s conflicts that can arise on an ongoing basis, such as by requiring the proxy advisory firm to update the investment adviser of business changes the investment adviser considers relevant ... or conflict policies and procedures.”<sup>13</sup>

The Advisers Act fiduciary duty, the Proxy Voting Rule, the Compliance Program Rule, and the Bulletin together provide a robust regulatory framework designed to ensure that advisers vote proxies in the best interest of their clients and conduct appropriate due diligence on third party providers. No further regulation of the adviser proxy voting process is warranted.

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<sup>9</sup> Rule 206(4)-7(b).

<sup>10</sup> See *SEC Staff Legal Bulletin No. 20, 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/cfsfb20.htm>.

<sup>11</sup> *Id.* at Answer to Question 3.

<sup>12</sup> *Id.* at Answer to Question 4 (reference omitted).

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

### **III. Additional Regulation of Proxy Advisory Firms that Would Increase the Cost of their Services for Advisers and their Clients, or Increase Barriers to Entry, is Not Warranted or Appropriate**

We strongly object to regulations that would increase the costs of proxy advisory firm services for advisers and their clients or raise barriers to entry for new proxy advisory firms. We do not believe such regulations are necessary and believe that any marginal benefit would be heavily outweighed by the adverse effect on access to these services for our members.

Some commentators point to conflicts of interest as grounds for regulation of proxy advisory firms. However, as discussed at the Roundtable, proxy advisory firms currently disclose their conflicts of interest transparently in a manner sufficient for investment advisers to review and evaluate them. Accordingly, this issue does not present a basis for a wholesale new and burdensome regulatory regime that would raise costs substantially and make it more difficult for other proxy advisory firms to enter the marketplace.

There have also been suggestions that proxy advisory firms should be required to distribute their reports to issuers to allow them to review and comment on the reports prior to their distribution to investment advisers and other users of these reports. While we certainly agree that factual accuracy of the reports is very important, we have two significant concerns with the solutions proposed. First, the discussion at the Roundtable highlighted that users of proxy advisory firm services do not necessarily want issuers interfering with the independence of the recommendations and analyses or influencing the content of the reports. Second, this approach is not likely to work in practice. In most cases, there will not be sufficient time to distribute reports to issuers, receive feedback from them, and then distribute reports to advisers and other users of these reports in time for them to vote. Indeed, the extremely tight timeline for the entire proxy voting process points to the need to address the process holistically as the first and highest priority.

### **IV. It is Neither Appropriate Nor Workable to “Pass Through” Votes Held by Funds to Fund Shareholders**

Separately from challenges to the services provided by proxy advisory firms, certain commentators have also suggested that funds obtain feedback directly from shareholders regarding proxies for fund portfolio securities, or “pass through” proxy votes for portfolio securities to fund shareholders. These suggestions are inappropriate and impractical and we do not believe they would benefit fund shareholders. Indeed they could harm the interests of fund shareholders. First, a primary reason that investors purchase fund shares – as opposed to individual securities – is to benefit from the professional portfolio management of the fund, and that includes proxy voting by the manager. An integral component of the benefit that an investor receives from investing in a fund is the expert analysis of the fund manager in making voting decisions that will enhance shareholder value. Second, fund shareholders currently have access to key information regarding fund proxy voting, including fund proxy voting policies and a fund’s voting history on each and every item on which it cast votes. A shareholder can choose to

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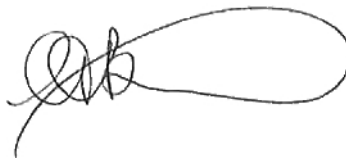
use that information to determine the funds in which to invest consistent with the shareholder's philosophy. We also note that a fund's portfolio securities are legally owned by the fund, not the fund's shareholders. Therefore, shareholder rights, including proxy voting, should be exercised by the fund as legal owner.

Finally, a fund may hold hundreds or thousands of securities. Distributing information to and collecting information from fund shareholders about votes regarding portfolio securities would be extremely costly and logistically very difficult, if not impossible to administer. The scope and scale of proxies, the number of shareholders, the difficulty in gathering and analyzing feedback that may or may not be clear, reconciling such feedback, and the extremely tight timeframe noted above, among other factors, render this concept entirely infeasible. Even if it were feasible, it would be enormously burdensome and confusing for shareholders, who would be overwhelmed with paperwork. These shareholders have made an affirmative decision to invest in a fund managed by professionals, rather than doing their own investment research. Proxy voting is part of that core portfolio management function that shareholders do and should expect to be handled by fund management.

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For the reasons discussed above, we believe that the Commission should deploy its limited resources to focus on how to improve and modernize the proxy infrastructure to ensure effective shareholder engagement and not take any actions that would undermine the ability of investment advisers to access critically important proxy advisory firm services. We commend the Staff for a successful Roundtable and appreciate the opportunity to provide comments on these important issues. Please do not hesitate to contact the undersigned or Sarah Buescher at (202) 293-4222 if we can be of further assistance.

Respectfully Submitted,

A handwritten signature in black ink, appearing to be 'GCB', written over a horizontal line.

Gail C. Bernstein  
General Counsel

cc: The Honorable Jay Clayton, Chairman  
The Honorable Kara M. Stein, Commissioner  
The Honorable Robert J. Jackson Jr., Commissioner  
The Honorable Hester M. Peirce, Commissioner  
The Honorable Elad L. Roisman, Commissioner  
Dalia Blass, Director, Division of Investment Management  
William Hinman, Director, Division of Corporation Finance