SHARE
SHAREHOLDER ASSOCIATION
for RESEARCH & EDUCATION

January 30, 2020

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

Re:

S7-23-19 Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a-8
S7-22-19 Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice

Dear Ms. Countryman,

I am writing to offer comment on the rules proposed by the Securities and Exchange Commission (SEC) on November 5th, 2019. Both proposals are arbitrary, costly, counter-productive and detrimental to the workings of capital markets and the private ordering of shareholder and management relationships.

These changes will undermine opportunities for shareholder input into effective corporate governance, severely limit shareholders' ability to advocate for investor interests and effective issuer risk management, and interfere with investor rights to unfiltered analysis and advice regarding their own private interests and the exercise of their rights. Further, the Commission's rule-making process in this instance has shown little regard for factual evidence nor demonstrated the required level of economic analysis regarding the need for, design of, and effects of either proposed rule.

The Shareholder Association for Research and Education ("SHARE") advises institutional investors with more than $23 billion in assets under management on environmental, social and governance (ESG) matters related to their portfolios. We regularly engage in discussions on corporate governance issues with boards and management of a wide range of issuers as well as a large cross-section of the North American institutional investor community.

Our clients are long-term shareholders that, through SHARE, regularly engage in dialogue with issuers to improve oversight, drive long-term performance and promote effective risk management. At times, we use the shareholder resolution process judiciously to raise issues that have not yet been effectively addressed by the company but which we believe are linked to better performance and risk management.

In addition, SHARE provides proxy voting recommendations to institutional investors based on guidelines adopted by those institutions, to assist them in fulfilling their fiduciary duties as investors.

The proposed changes were based on fictitious letters, tainting the whole process

When introducing the proposed rule changes, SEC Chair Jay Clayton was quoted as saying that the proposals stemmed from concerns expressed in letters from "main street investors". "Some of the letters that struck me the most," he said, "came from long-term Main Street investors, including an Army veteran and a Marine veteran, a police officer, a retired teacher, a public servant, a single mom, a couple of retirees who saved for retirement."[1] Many of these comment letters, however, turned out to be written by a lobbyist organization, and some of their alleged authors denied ever seeing the letters.

The reliance upon potentially fraudulent letters suggests that the SEC's process in this instance is arbitrary and capricious and violates the requirement that SEC rules be based on a rational review of existing evidence. The SEC has indicated it intends to review the situation. But when the rationale for adopting new rules is based on information that turns out to be fabricated, the integrity of the process – and the need for new rules at all – is undermined. This review process itself should be abandoned. Instead, the SEC should start by asking whether changes to existing rules are in fact useful or desired by any actual investors, and if so revisit the issue with an adequate factual and economic analysis.

The Commission failed to adequately assess the impact of the proposed changes to the proxy advisory rules

The Commission's proposal on proxy advisory rules provides little evidence of the kind of analysis required by the Commission's own rule-making procedure.[2] For example:

- **There is no significant evidence of faulty advice:** The Commission cites registrants "perception" of factual errors in proxy advisor recommendations, and notes that in 2018 there were 17 such "factual errors" and 28 "analytical errors" cited by registrants. The Commission does not evaluate whether in fact the "factual errors" and "analytical errors" cited by companies were in fact errors at all, or just differences of opinion or problems with the company's own disclosures. Even if they were *actual* and not just *alleged* errors, given that proxy advisors typically produce thousands of reports each year with tens of

[1] https://www.sec.gov/news/public-statement/statement-clayton-2019-11-05-open-meeting
[2] https://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf

thousands of data points, the statistical significance of these alleged errors is nil. It would be unthinkable to impose massive costs on proxy advisors, and ultimately on investors and pension beneficiaries, on the basis of an unexamined claim of a statistically insignificant level of alleged errors. But this is exactly what the Commission is now proposing to do.

- **There is no evidence that any errors affected voting decisions:** Further, the Commission offers no evidence to suggest that these errors, if they are even confirmed to be errors and not just disagreements in interpretation, were actually material to investors' voting decisions. If the alleged errors in question had little or no effect either on the actual vote recommendation provided, the rationale for intervening in proxy advisory processes would be completely unfounded. And even if the alleged errors in question affected the vote recommendation, did they influence the vote decisions taken by investors (who in our experience do not follow the recommendations of proxy voting services consistently and unquestioningly)? If not, the rationale for intervening in proxy advisory processes would again be completely unfounded.

- **The costs imposed on main street investors are not justified**: The Commission acknowledges that it has no data to determine the costs of requiring proxy advisory firms to solicit feedback from companies about any proxy advice to be provided to their clients. The cost of added resources to comply with this rule will ultimately be borne by investors and main street pension beneficiaries whose retirement savings will be affected by any added fees associated with compliance. Prior to affecting retirees' future income, shouldn't the Commission should conduct a more thorough review of real costs, and determine whether 17 alleged "factual errors" per year is worth the cost those retirees would incur?

- **There is no evidence for the assumed benefit of these rules**: The Commission mused that "by establishing requirements that promote accuracy and transparency in proxy voting advice, the proposed amendments could lead to an increased demand for voting advice from proxy voting advice businesses." It makes this assertion with no indication from actual investors – aside from the phony investors put forward by corporate lobbyists and unduly relied upon by the Commission – that there is any material concern with the factual accuracy of the voting recommendations received, that investors are holding back from purchasing advice because of these concerns, or that allowing corporations to intervene in the advice being produced will heighten (rather than weaken) the investors' confidence in the recommendations provided. To posit this evidence-free wishful thinking as an economic "benefit" and/or counterpoint to the significant real costs being imposed is misleading at best.

- **The new rules are anti-competitive**: That the Commission then relies upon this same evidence-free wishful thinking as a basis for asserting that "the proposed amendment could lead to increased demand for proxy voting advice business services [and that] increased demand for their services could, in turn, lead to increased competition among proxy voting advice businesses to meet that increased demand" compounds the error. There is no basis for this claim. In fact, the opposite is true. The Commission acknowledges that the additional cost of complying with this rule could further entrench the moat that is built up around the proxy advisory business, which is almost entirely dominated by two corporations. The additional costs would limit the ability of competitors to enter the market. As a small firm that offers proxy advisory services to institutional investor clients, we can attest to the significant hurdle that additional technological, logistical and personnel costs associated with compliance would create for smaller organizations like ours, further limiting our ability to compete at scale. In effect, the Commission's effort to address an alleged 17 "factual errors" may solidify a duopoly in American business and prevent any future entrants from gaining a toehold. This, in turn, could affect the prices paid by investors for these services due to lack of competition, creating additional costs again to be paid for by reductions in retirees' savings.

While we oppose the proposed rule changes in their entirety, we would at minimum support the Commission's suggestion that smaller firms might be exempted from the rules in order to foster a competitive marketplace.

Thus we oppose the Commission's proposed new requirements for proxy advisory services on the basis that the new rules will have an anti-competitive effect in the market and are based on questionable and insufficient evidence that, even if it were found to be true, would indicate a minor error in a few proxy vote recommendations that is infinitesimally tiny relative to the scale of the industry, and that has with no demonstrated material effect on the voting decisions made by investors.

Further, we share the concern stated by many of the commentators that proxy advisory services are providing a service to investors, not issuers, and the reliability and usefulness of that advice is to be judged by the private clients purchasing those services. This should not be a matter for regulatory action, short of the existing requirements that already govern their activities.

The Commission's proposed changes to the shareholder proposal rules will disenfranchise investors and damage shareholder value

We have commented in a separate letter[3] on some of the effects of the Commission's proposed rules to limit investors' use of representatives to file shareholder proposals and to engage with

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[3] January 27, 2020, letter co-signed with Timothy Smith Director, ESG Shareowner Engagement, Boston Trust Walden), Michael W. Frerichs (Treasurer, State of Illinois), Scott M. Stringer (New York City Comptroller), Danielle Fugere (President, As

corporate management, as well as the requirement for shareholders to hold time available for corporate engagement without any requirement on the issuer to take advantage of that opportunity to engage.

In addition to those concerns, we raise the following:

- **The new rules disenfranchise smaller and main street investors**: By the Commission's own admission, the proposed new submission thresholds "could have a greater effect on retail investors compared to institutional investors because the average holdings of retail investors are typically lower than the average holdings of institutional investors." This is also true for smaller institutional investors. Compounding this effect, the Commission proposes to arbitrarily curtail the ability of smaller shareholders to aggregate their shares to meet the thresholds, which seems completely out of step with its own argument that ownership thresholds are meant to limit the process only to those with an economic stake in the firm – stakes that could equally be demonstrated by a group of investors who collectively seek to engage management.

  Disenfranchising smaller investors, whether retail or institutional, responds only to the desire by some corporate CEOs and lobbyists to be less accountable to shareholders overall. There is no evidence that the concerns raised by smaller shareholders are less relevant, material, or valuable than those of larger shareholders. Thus, the proposed changes to the minimum ownership thresholds for filing proposals are arbitrary and incomprehensible.

- **There is very little *abuse* of the process, especially compared to its *use***: The sole intelligible purpose for these changes expressed in the Commission's proposal is to prevent abuse of the process by shareholders with a limited interest in the success of the company. With respect, the evidence of abuse of the process is slim at best, any existing abuse of the process would be extraordinarily small compared to the number of relevant, material and valuable proposals that will be arbitrarily excluded under the new rules. Any abuse of the process is already adequately limited by the SEC's own no-action request process as well as – most appropriately – by the exercise of the shareholder vote, which ultimately rejects proposals with no relevance, materiality or value to the company.

- **Limiting the re-submission of proposals will kill good ideas in the womb**: There is no demonstrable need for new rules to limit resubmission of shareholder proposals. In fact, the system as it is currently devised is working well. Proposals that do not meet approval from shareholders are, over time, revised or eliminated. Yet the current system also allows the time for shareholders and corporate management to better understand and consider

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You Sow), Susan Smith Makos (Vice President of Social Responsibility, Mercy Investment Services), Brandon Rees (Deputy Director, Corporations and Capital Markets, AFL-CIO) and Bruce T. Herbert (Chief Executive, Newground Social Investment) the implications of good proposals that may, at first, garner lower vote results. According to a more comprehensive evaluation of resubmission rates by the Sustainable Investments Institute (Si2) based on a database of 4,300 Environmental, Social and Governance (ESG) resolutions voted on from the beginning of 2010 through Nov. 18, 2019, 614 ESG-related resolutions, or about 30%, of the 2,019 proposals voted on at company annual meetings over that period would not have been eligible for resubmission under the proposed new rules.[4]

Evidence of the importance of resubmission has been presented by multiple commenters, so we won't repeat it here. However, it is clear from our own experience as filers of multiple constructive shareholder proposals (on behalf of our institutional investor clients), that proposals which started with low levels of shareholder support often become accepted wisdom amongst boards, shareholders and regulators, given time. Our proposals result in positive changes in corporate governance and behavior that mitigate risks for our clients and contribute to outperformance. Cutting that process short by allowing companies to exclude proposals that are not immediately understood and widely accepted will kill many critical, constructive and necessary ideas in the womb.

Further, the proposed re-submission thresholds will limit an essential risk-management tool for institutional investors at the very time those tools are needed most. While the Commission did no economic analysis of the potential risk to shareholder value of blocking shareholder proposals on ESG concerns, others have. Most recently, for example, the Bank of America estimated the loss to shareholder value of ESG controversies within the last five years at companies on the S&P 500 Index was more than US $500 billion.[5]

- **Changes to re-submission thresholds will further entrench management**: Concerns over re-submission thresholds are amplified for firms with dual-class share ownership or otherwise controlled companies. The percentage of dual-class share companies has increased over the last decade, and seven of the largest ten IPOs in 2019 included dual-class structures.[6] Within that context, raising resubmission thresholds exacerbates an existing entrenchment of management and further disenfranchises shareholders, especially at those companies that may be most in need of governance improvements and accountability to shareholders.

With respect, both sets of proposed rules do nothing to enhance productive dialogue between shareholders and corporate management and do nothing to assist investors in accurately and carefully executing their voting responsibilities. Rather, the proposed rules do tremendous damage

[4] https://www.investorrightsforum.com/new-blog-1/sampp-sec-proposed-rule-would-have-blocked-614-esg-resolutions-since-2010-data-showsnbsp
[5] https://www.ft.com/content/3f1d44d9-094f-4700-989f-616e27c89599
[6] https://corpgov.law.harvard.edu/2019/06/28/dual-class-shares-governance-risks-and-company-performance/

to the confidence investors can place in the smooth functioning of US capital markets. Were they to be enacted –despite the Commission's marked failure to properly evaluate their impacts on investors, to appropriately address their anti-competitive effects, to adequately consider the material benefits for both investors and corporations of the current shareholder proposal process, and to accurately portray the role of proxy advisory services – they would undermine the very rights and responsibilities that shareholders and fiduciaries rely upon to protect their investments and those of their beneficiaries.

We ask, therefore, that the proposed changes articulated in *File Number S7-23-19: Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a-8* and in *File Number S7-22-19: Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice* be scrapped in their entirety.

Best regards,

Kevin Thomas
Chief Executive Officer
Shareholder Association for Research & Education (SHARE)