

SEC Adopts Amendments to Proxy Solicitation Rules and Issues Related Guidance

I. Overview

On July 22, 2020, the Securities and Exchange Commission (the “SEC”) voted to adopt amendments¹ to the proxy solicitation rules intended to provide “more transparent, accurate, and complete information” to investors when making voting decisions. The final amendments summarized below follow the SEC’s proposed amendments to the proxy solicitation rules published in November 2019 (the “Proposing Release”), which included, among others, proposals (1) to codify the SEC’s long-standing interpretation that proxy voting advice generally constitutes a solicitation within the meaning of Section 14(a) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), (2) to condition the availability of certain exemptions from the information and filing requirements relied on by proxy advisors upon satisfaction of additional disclosure and procedural requirements, and (3) to amend the Exchange Act Rule 14a-9 to clarify that the failure to disclose certain information in proxy voting advice may be considered materially misleading. With the Adopting Release, the SEC also concurrently issued supplemental guidance to assist investment advisers with respect to their proxy voting responsibilities, as summarized below.²

II. Codification of the SEC’s Interpretation of “Solicitation” (Rule 14a-1(l) and Section 14(a))

Under Section 14(a) of the Exchange Act, it is unlawful for any person to “solicit” any proxy with respect to any security registered under Section 12 of the Exchange Act in contravention of such rules and regulations. However, the term “solicitation” for purposes of Section 14(a) and the proxy rules is not defined in the Exchange Act. Under the Proposing Release, the SEC proposed to clarify that the terms “solicit” and/or “solicitation” should:

- include any proxy voting advice that makes a recommendation to a shareholder as to its vote, consent, or authorization on a specific matter for which shareholder approval is solicited, and that is furnished by a person who markets its expertise as a provider of such advice, separately from other forms of investment advice, and sells such advice for a fee;
- include voting recommendations formulated pursuant to a proxy advisory firm’s client’s own custom policies; and
- exclude any proxy voting advice furnished by a person who furnishes such advice only in response to an unprompted request.

In the Adopting Release, the SEC adopted all of the above substantially as proposed.

¹ For the full text of the final rule and the related SEC release, see Securities and Exchange Commission, Exemptions from the Proxy Rules for Proxy Voting Advice, SEC Release No. 34-89372; File No. S7-22-19, available at <https://www.sec.gov/rules/final/2020/34-89372.pdf> (July 22, 2020) [hereinafter, the “Adopting Release”].

² For the full text of the supplemental guidance and the related SEC release, see Securities and Exchange Commission, Supplement to Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers, SEC Release No. IA-554, available at <https://www.sec.gov/rules/policy/2020/ia-5547.pdf> (July 22, 2020) [hereinafter, the “Supplemental Guidance”]. Unless otherwise specified, quoted statements in this memorandum are taken from the Adopting Release and the Supplemental Guidance, as the context suggests.

III. Conflicts of Interest (Rule 14a-2(b))

Given the risk that the proxy advisory firm's voting advice could be influenced by the firm's own interests, the Proposing Release included a proposed amendment that would require persons who provide proxy voting advice to include the following disclosures:

- Any material interests, direct or indirect, of the proxy advisory firm (or its affiliates) in the matter or parties concerning which it is providing the advice;
- Any material transaction or relationship between the proxy advisory firm (or its affiliates) and (1) the company (or any of the company's affiliates), (2) another soliciting person (or its affiliates), or (3) a shareholder proponent (or its affiliates), in connection with the matter covered by the proxy voting advice;
- Any other information regarding the interest, transaction, or relationship of the proxy advisory firm (or its affiliates) that is material to assessing the objectivity of the proxy voting advice in light of the circumstances of the particular interest, transaction, or relationship; and
- Any policies and procedures used to identify, as well as the steps taken to address, any such material conflicts of interest arising from such interest, transaction, or relationship.

Although the SEC adopted the amendments above substantially as proposed, the Adopting Release established a principles-based requirement based on a standard of materiality. As such, anyone providing proxy voting advice who wishes to utilize the exemption from the information and filing requirements pursuant to Rule 14a-2(b)(1) or (b)(3), must include in its voting advice (or in any electronic medium used to deliver the advice) prominent disclosure of the following, which cannot be boilerplate language:

- Any information regarding an interest, transaction, or relationship of the proxy advisory firm (or its affiliates) that is material to assessing the objectivity of the proxy voting advice in light of the circumstances of the particular interest, transaction, or relationship; and
- Any policies and procedures used to identify, as well as the steps taken to address, any such material conflicts of interest arising from such interest, transaction, or relationship.

IV. Notice of Proxy Voting Advice and Response (Rule 14a-2(b))

In an effort to enhance transparency, accuracy, and completeness of proxy voting advice, the SEC proposed in the Proposing Release to impose certain conditions that proxy advisory firms would have to satisfy when relying on the exemption from the information and filing requirements pursuant to Rule 14a-2(b)(1) or (b)(3). Under the Proposing Release, among other things, (1) a proxy advisory firm would be required to provide companies and certain other soliciting persons covered by its proxy voting advice a limited amount of time to review and provide feedback on the advice before it is disseminated to the firm's clients, and (2) companies and certain other soliciting persons would be given the option to request that proxy advisory firms include in their proxy voting advice a hyperlink or other analogous electronic medium directing the recipient of the advice to a written statement prepared by the company (or other soliciting person, as applicable) setting forth its own views.

The amendments as adopted differ from the proposals in the Proposing Release and adopt a less prescriptive and more principles-based approach. Specifically, the Adopting Release provides that a proxy advisory firm is required to adopt and publicly disclose written policies and procedures to rely on the exemptions in Rules 14a-2(b)(1) and (b)(3). Such policies and procedures must be reasonably designed to ensure that (1) companies that are the subject of proxy voting advice have such advice made available to them at or prior to the time such advice is disseminated to the proxy advisory firm's clients, and (2) the proxy advisory firm provides its clients with a mechanism by which they can reasonably be expected to become aware of any written statements regarding its proxy voting advice by companies that are the subject of such advice in a timely manner before the shareholder meeting.

The final rules also include two non-exclusive safe harbors which allow proxy advisory firms to ensure that their written policies and procedures satisfy the new requirements described above. The first requirement in the preceding paragraph would be deemed satisfied if the policies and procedures are reasonably designed to provide companies with a copy of the proxy voting advice, at no cost, to the clients. Such policies and procedures may include conditions, such as requiring a company to (i) file its definitive proxy statement at least 40 calendar days before the shareholder meeting, and (ii) expressly acknowledge that the company will only use the proxy voting advice for its own internal purposes and/or in connection with the solicitation and it will not publish or share the proxy voting advice except with its own employees or advisers. The second requirement in the preceding paragraph will be deemed satisfied if the policies and procedures are reasonably designed to provide notice on an electronic client platform or through email or other electronic means, that a company has filed, or has informed the proxy advisory firm that it intends to file, additional soliciting materials (and includes in such notice an active hyperlink to those materials on EDGAR when available).

V. Anti-Fraud Provisions (Rule 14a-9)

Rule 14a-9 prohibits any proxy solicitation from containing false or misleading statements with respect to any material fact at the time and in light of the circumstances under which the statements are made. In addition, such solicitation must not omit to any material fact necessary to make the statements not false or misleading.

In the Proposing Release, the SEC proposed to amend the list of examples in Rule 14a-9 of things that may be misleading within the meaning of the rule, to include certain additional types of information that a proxy advisory firm may, depending on the particular facts and circumstances, need to disclose to avoid potentially violating the rule, including the proxy advice firm's methodology, sources of information and/or conflicts of interest to the extent that, under the particular facts and circumstances, the omission of such information would be materially misleading. In addition, the SEC proposed to add as an example the failure to disclose the use of standards or requirements in proxy voting advice that materially differ from relevant standards or requirements of the SEC.

Although the SEC adopted the amendments in the Proposing Release largely as proposed by adding a new paragraph which would include as examples the proxy advisory firm's methodology, sources of information, or conflicts of interest that could, depending upon particular facts and circumstances, be misleading, the SEC did not adopt the proposed addition regarding the failure to disclose the use of standards or requirements that materially differ from relevant standards or requirements of the SEC.

VI. Supplemental Guidance Regarding Investment Advisers

In addition to the Adopting Release, the SEC supplemented its prior guidance with respect to the proxy voting responsibilities of investment advisers, in light of the additional information that may become available



as a result of the amendments described above. In the Supplemental Guidance, the SEC addressed situations where a proxy advisory firm assists its clients, including investment advisers, with voting execution through an electronic vote management system.

The prior guidance discussed the steps that an investment adviser could take to demonstrate that its voting determinations are being made in a client's best interest, such as assessing pre-populated votes shown on the proxy advisory firm's electronic voting platform and considering additional information that may become available before the vote. The Supplemental Guidance provides that in addition to the above, an investment adviser should (1) consider whether its policies and procedures, such as policies and procedures with respect to automated voting of proxies, are reasonably designed to ensure that it exercises voting authority in its client's best interest (for example, whether the policies and procedures address situations where the investment adviser becomes aware that a company filed or will file additional soliciting materials after it has received a voting recommendation from a proxy advisory firm), and (2) in light of the non-public information that proxy advisors may come to possess regarding how an investment adviser plans to vote a client's securities, consider reviewing its agreements with proxy advisory firms to determine whether the agreements permit the proxy advisory firms to use the information in a manner that would not be in the best interest of its client. The Supplemental Guidance provides that if an investment adviser uses automated voting, it should further consider: (a) disclosing the extent of that use and under what circumstances it uses automated voting, (b) disclosing how its policies and procedures address the use of automated voting in cases where it becomes aware before the submission deadline for proxies to be voted that a company has filed or will file additional soliciting materials, and (c) whether its policies and procedures are reasonably designed to address these disclosures.

VII. Conclusion

The amendments will become effective 60 days following their publication in the Federal Register. However, the final rules provide for a one-year transition period after the publication of the final rules to give proxy advisors sufficient time to develop any necessary processes and systems to comply with the new rules. Proxy advisors will not be required to comply with the amendments to Exchange Act Rule 14a-2(b)(9) until December 1, 2021. The Supplemental Guidance will become effective upon publication in the Federal Register.

In the Adopting Release, the SEC stated that although it does not believe it is necessary to subject proxy advisory firms to the information and filing requirements applicable to registrants, given the role of proxy advisory firms in today's market the new rules should facilitate adequate disclosure and enable the firms' clients to have "reasonable and timely access to transparent, accurate, and complete information material to matters presented for a vote." The heightened disclosures and requirements, although less prescriptive than the amendments as proposed in November 2019, nonetheless appear on their face to provide greater flexibility for the proxy advisory firms and increased transparency and engagement opportunities for other stakeholders.

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email authors Geoffrey E. Liebmann at 212.701.3313 or gliebmann@cahill.com; or Joseph E. Cho at 212.701.3589 or jcho@cahill.com; or email publications@cahill.com.