

PROXY SEASON SURVEY

2020



CENTER FOR CAPITAL MARKETS
COMPETITIVENESS®



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Presented by:



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The U.S Chamber of Commerce’s Center for Capital Markets Competitiveness (CCMC) and Nasdaq have again partnered to conduct our annual proxy season survey. This survey examines the interactions that public companies had with proxy advisory firms during the 2020 proxy season and is intended to inform policymakers and the general public about current practices within the proxy advisory industry.

Proxy advisors play an important role within the corporate governance ecosystem in the U.S. They analyze corporate governance matters at public companies and develop voting recommendations for institutional investors that are tasked with voting proxies in the best interests of Main Street investors. Given the thousands of proxy issues that institutional investors must consider in any given year, a well-functioning proxy advisory system helps ensure that votes are always cast in a manner that enhances the long-term performance of public companies.

However, the proxy advisory system has operated for years with a number of serious flaws. The industry is effectively controlled by two firms—Institutional Shareholder Services (ISS) and Glass Lewis—that make up over 90% of the market, giving them extraordinary influence over corporate governance standards. These two firms also have a history of being prone to making errors when drafting

vote recommendations and operate with significant conflicts of interest. These deficiencies have led to bipartisan calls for reform in Congress and a thorough examination of industry practices by the Securities and Exchange Commission (SEC) over the last decade.

In July 2020, the SEC finalized a rulemaking that will make the proxy advisory industry more transparent and enhance the quality of vote recommendations received by institutional investors.¹ The rule codifies the long-standing position of the SEC that proxy advice constitutes a “solicitation” under the federal proxy rules and establishes a mechanism for public companies to review draft vote recommendations in order to correct any errors or analytical flaws. The rule will also result in more robust disclosures regarding proxy advisory firm conflicts of interest. The SEC concurrently issued Commission-level guidance clarifying the duties of institutional investors that hire proxy advisory firms.² The guidance affirms that it would be a breach of fiduciary duty for an institutional investor to automatically rely on proxy advisor vote recommendations without performing its own due diligence and conducting sufficient oversight of a proxy advisory firm it has hired.

Additionally, the Department of Labor (DOL) recently proposed a rule regarding the proxy voting duties of fiduciaries under the Employee Retirement Income Security Act (ERISA).³ The DOL’s rule would, among other provisions, require that ERISA fiduciaries take steps to affirm that the proxy advisory firms they hire have the ability to provide objective and informed voting advice and that recommendations are not tainted by conflicts of interest. The proposal would also reiterate that fiduciaries are never allowed to subordinate the economic interests of ERISA plan participants to non-pecuniary factors when voting proxies.

These regulatory actions have been informed by several SEC roundtables, requests for public comment, numerous academic studies, congressional hearings, and other forums stretching back over the last decade that have explored problems with proxy advisory firms along with potential reforms.

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1. Exemptions from the Proxy Rules for Proxy Voting Advice (July 22, 2020).
 2. Supplement to Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers (July 22, 2020). Do you mean Supplement?
 3. Fiduciary Duties Regarding Proxy Voting and Shareholder Rights (August 31, 2020).

The CCMC and Nasdaq have long supported changes to the regulatory framework that applies to the proxy advisory industry. In May 2017, Nasdaq made proxy advisory reform a cornerstone of its blueprint to revitalize the capital markets.⁴ We believe reforms are necessary to improve the public company model in the U.S. and help stem the drastic decline in public companies that has occurred over the last two decades. Fewer public companies translate to lower economic growth, less job creation, and fewer opportunities for Main Street investors to own the next generation of great American businesses.

This is the sixth year that the CCMC and Nasdaq have conducted the proxy season survey. A record 182 companies participated in this year's survey, which was conducted during the months of July and August. Participants included public companies of all sizes that cut across virtually every sector of the U.S. economy.

4. The Promise of Market Reform Reigniting America's Economic Engine (May 2017). Available at https://www.nasdaq.com/docs/Nasdaq_Blueprint_to_Revitalize_Capital_Markets_April_2018_tcm5044-43175.pdf

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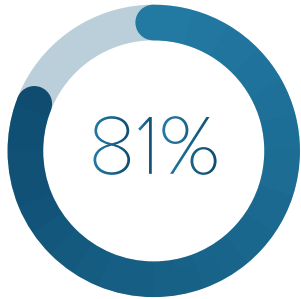
The survey found that companies overwhelmingly support the ability to “review-and-comment” on draft proxy advisory firm recommendations, and the vast majority of companies were aware and supportive of the SEC’s rulemaking regarding proxy advisory firms. Over 80% of the companies believe that the review-and-comment mechanism contained in the SEC rulemaking would result in better informed voting decisions by SEC-registered investment advisers.

The survey also found that responsiveness and transparency on behalf of proxy advisory firms continues to decline. Over the last four years, proxy advisory firms have become increasingly likely to deny a request from a public company to meet or discuss a particular vote recommendation.

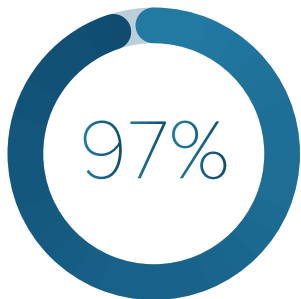
Troublingly, and consistent with the 2019 survey, over half of the companies report that they have been approached by the corporate consulting arm of ISS during the same year in which they received a negative vote recommendation from ISS’ proxy advice business. The ISS business model—in which it provides corporate governance consulting to the very issuers for which it issues vote recommendations—is inherently conflicted and creates potential biased voting advice. The recently adopted SEC rule should help public companies and investors better understand how particular vote recommendations may be improperly influenced by ISS business considerations.

SURVEY RESULTS

Public Companies Overwhelmingly Support Aspects of the SEC's Rulemaking

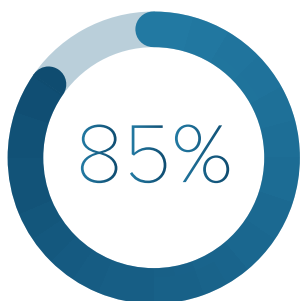


81% of the companies reported that they were aware of the SEC rulemaking related to proxy advisory firms, with 99% of those companies saying they support the rule.

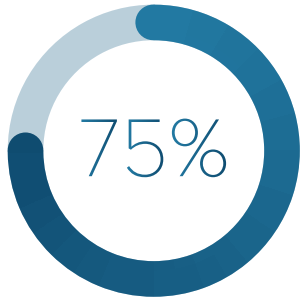


97% of the companies reported that they would avail themselves of the review-and-comment mechanism included in the SEC rule; interestingly, 85% said that such a mechanism would not create any unnecessary delays or confusion in the proxy voting process.

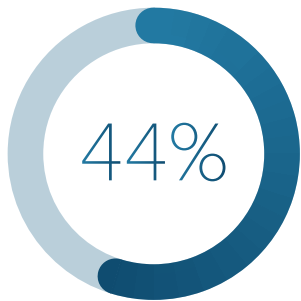
Public Company Engagement With Proxy Advisory Firms: Ability to Communicate With Proxy Advisory Firms Remains a Significant Challenge



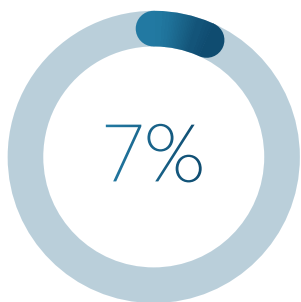
85% of the companies surveyed had a proxy advisory firm make a recommendation regarding an issue included in their proxy statement, a level slightly lower than in 2019 (87%) and 2018 (92%).



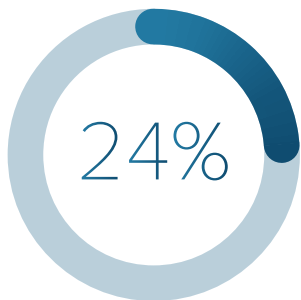
75% of the companies carefully monitor proxy advisory firm recommendations for accuracy or reliance on outdated information, a lower number than in 2019 (80%) and 2018 (83%).



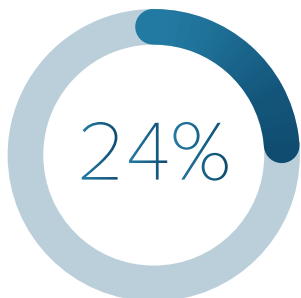
Only **44% of the companies responding believe that proxy advisory firms carefully research and consider all relevant aspects of a particular issue** on which it provides advice, higher than in both 2019 and 2018 (39% both years).



7% of the companies formally requested that proxy advisory firms provide them with a preview of vote recommendations, continuing a declining trend from 2019 (17%), 2018 (21%), and 2017 (30%).

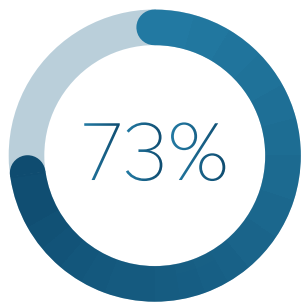


The number of companies asking proxy advisory firms for the opportunity to provide input before a vote recommendation is finalized continues to decline. In 2020, **24% of companies made such a request**, down from 30% in 2019 and 38% in 2018.

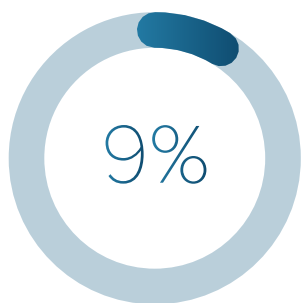


24% of the companies pursued opportunities to meet with proxy advisory firms on issues subject to shareholder votes, up from 21% in 2019 but down from 29% in 2018. For companies that asked for a meeting, that request was denied 69% of the time. This is the fourth year that the denial rate has increased, up from 60% in 2019, 57% in 2018, and 38% in 2017.

Public Company Engagement With Investors and the SEC



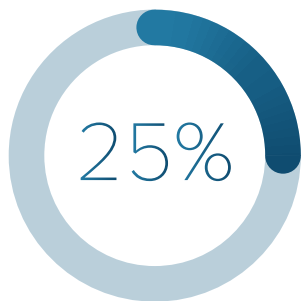
While a majority **(73%) of the companies reported that they have in place a year-round regular communications program with institutional investors**, that number is down from 2019 (82%) and 2018 (78%). Companies that have such a program in place believe it is particularly beneficial for proxy-related matters.



If a company reported that it was not granted adequate opportunities for input on a proposed proxy advisor vote recommendation, **it notified proxy advisory firms and portfolio managers 9% of the time**, a sharp decline from 23% in 2019.

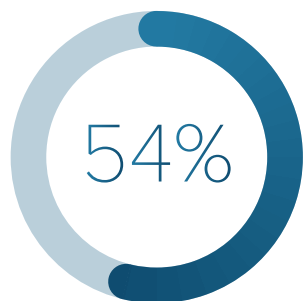


If a company encountered a vote recommendation it believes was based on inaccurate or stale data, **it alerted the proxy advisory firm, institutional investors, and/or the SEC staff 25% of the time**, down from 41% in 2019 and 46% in 2018.



25% of the companies advised proxy advisory firms and their clients if a recommendation did not advance the best economic interests of shareholders, down from 29% in 2019.

Conflicts of Interest



A troubling **54% of the companies reported that they were approached by a representative of ISS Corporate Solutions during the same year in which they received a negative vote recommendation from ISS.** This is similar to last year when 58% of the companies reported they were contacted by ISS Corporate Solutions.

Shares Voted Automatically In Line With Proxy Advisory Firms



For the last three years, this survey has sought to learn whether a significant portion of an issuer's shares are "robot-voted" in line with an ISS or Glass Lewis recommendation within 48 hours of that recommendation being issued. As in 2018 and 2019, several companies reported that anywhere from 20%–35% of their shares are voted automatically with proxy advisory firms once vote recommendations are issued.

PROXY ADVICE BEST PRACTICES

The three constituency groups affected by the recently issued SEC guidance—proxy advisory firms, portfolio managers, and public companies—must focus their attention on five overarching principles:

Fiduciary duty

Fiduciary duties permeate and govern all aspects of the development, dispensation, and receipt of proxy advice. Some investors use proxy advisory reports as one data point among many in an independent process to determine how or when they should vote their shares. Unfortunately, other investors may still outsource their voting to proxy advisory firms without any due diligence.

Shareholder value

Enhancing and promoting shareholder value must be the core consideration in rendering proxy voting advice and in making proxy voting decisions.

Freedom from conflicts

The proper role of proxy advisory firms vis-à-vis proxy voting is to provide accurate and current information to assist those with voting power to further the economic best interests of those who entrust their assets to portfolio managers and are the beneficial shareholders of public companies. If proxy advisory firms exceed that role—for example, by effectively exercising or being granted a measure of discretion over how shares are voted on specific proposals, or by failing to make proper disclosure regarding specific conflicts of interest afflicting a proxy advisory firm in connection with voting recommendations it is making—the proxy advisory firms so employed, and those engaging them, incur serious legal and regulatory consequences. The recently adopted SEC rule will increase information regarding conflicts of interest, while the July 2020 Commission guidance suggests that institutional investors should conduct proper oversight of proxy advisory firms that they hire.

Portfolio manager discretion

Clarity is provided regarding the scope of portfolio managers' obligations to exercise a vote on proxy issues, and the obligations emphasize the broad discretion portfolio managers have—subject to appropriate procedures and safeguards—to refrain from voting on every, or even any, proposal put before shareholders for a vote.

Compliance

In light of the newly adopted SEC rule and Commission guidance, proxy advisory firms and portfolio managers need to again reassess their current practices and procedures and adopt appropriate changes, while public companies should be aware of these actions and how they will impact proxy voting.



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