UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF TENNESSEE
NASHVILLE DIVISION

CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA, BUSINESS ROUNDTABLE, and TENNESSEE CHAMBER OF COMMERCE & INDUSTRY,

Plaintiffs,

v.

SECURITIES AND EXCHANGE COMMISSION and GARY GENSLER, in his official capacity as Chairman of the Securities and Exchange Commission,

Defendants.

Civil Action No. 3:22-cv-00561
Judge Aleta A. Trauger
Magistrate Judge Jeffery S. Frensley

ORAL ARGUMENT REQUESTED

PLAINTIFFS' MEMORANDUM IN SUPPORT
OF THEIR MOTION FOR SUMMARY JUDGMENT

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INTRODUCTION

This case is about a highly unusual agency rulemaking that violated both the procedural and substantive requirements of the federal Administrative Procedure Act (APA) to the detriment of public companies and their shareholders. The shareholders of publicly traded companies are asked to vote on tens of thousands of proposals each year addressing all manner of corporate governance topics. Lacking the time or resources to analyze each issue themselves, many investors have turned to Proxy Voting Advice Businesses (PVABs) for advice on voting, which typically occurs "by proxy" as opposed to in person at the shareholder meeting. Those investors—who control trillions of dollars in companies' shares—often permit PVABs not just to advise but to actually cast their votes, through a process called "robo-voting," thus turning PVAB advice directly into corporate policy. As a result, PVABs have gained incredible influence over shareholder-voting decisions and the securities markets. But with little competition in the PVAB industry, deficiencies emerged with PVABs' advice. In particular, PVAB recommendations are often tainted by undisclosed conflicts of interest and inaccurate or incomplete information, yet the companies that are the subjects of this error-ridden or misleading advice have no means of offering timely responses that will reach shareholders prior to a vote.

After a decade of bipartisan study, the Securities and Exchange Commission issued a rule in 2020 imposing modest restrictions on PVABs, along with accompanying guidance (2020 Rule and 2020 Guidance). The 2020 Rule required PVABs to do two things aimed at bringing transparency to the proxy process. First, PVABs had to disclose their conflicts of interest. Second, PVABs had to provide their recommendations to companies and clients at the same time, and then alert their clients to any written response by the companies to those recommendations. But before the 2020 Rule could even go into effect, a new majority on the

Commission abruptly changed course. The Commission halted the 2020 Rule's implementation and then—after an abbreviated public comment period and without any reasoned explanation—issued the 2022 Rule, rescinding the requirement that PVABs provide their advice to subject companies and alert their clients to any responses to errors or incomplete information.

The APA protects the public against exactly this sort of regulatory whiplash by barring agencies from engaging in rulemaking that is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." 5 U.S.C. § 706(2)(A). Here, the Commission's unjustified rule reversal was unlawful under the APA for no fewer than five reasons.

First, the Commission promulgated the 2022 Rule through an inadequate 30-day comment period. To ensure that agencies engage in informed decisionmaking, the APA requires that agencies remain "open-minded" and provide a "meaningful opportunity" for public comment during the rulemaking process. *Rural Cellular Ass'n* v. *FCC* 588 F.3d 1095, 1101 (D.C. Cir. 2009). Rather than provide a meaningful opportunity for public participation, however, the Commission raced toward a predetermined outcome. The 30-day comment period was patently inadequate: it was half that provided for the 2020 Rule and also overlapped with the year-end holidays and financial reporting period; it violated the Commission's self-professed policy of always giving market participants at least two months to comment; and it contravened well-established Executive Branch practice. As explained below, courts have consistently vacated rules based on the comment period's inadequacy. The same course is warranted here.

Second, the Commission failed to provide a reasoned explanation (or any explanation) for disregarding its own factual findings underlying the 2020 Rule. Although agencies are not prohibited from changing course, they must provide a "reasoned explanation" rather than "a summary discussion" to explain why it was "necessary" to "overrule [a] previous position."

Encino Motorcars, LLC v. *Navarro*, 579 U.S. 211, 221 (2016) (agency policy reversal was arbitrary and capricious). Here, the Commission failed to provide a reasoned explanation for flip-flopping positions within a span of two years despite the unchanged factual record. Instead, the Commission embraced, without *any* explanation, arguments that it had already rejected during the 2020 rulemaking and offered conclusions that ran "counter to the evidence before the agency." *Nat'l Ass'n of Home Builders* v. *Defenders of Wildlife*, 551 U.S. 644, 658 (2007).

Third, the Commission failed to fulfill its statutory obligation under the Exchange Act to conduct a robust economic analysis of the 2022 Rule. *See Bus. Roundtable* v. *SEC*, 647 F.3d 1144, 1148 (D.C. Cir. 2011) (Commission's failure to adequately "assess the economic effects of a new rule" rendered rule arbitrary and capricious). Instead of offering an "adequate" economic assessment, the Commission presented an internally inconsistent analysis that "opportunistically fram[ed] the costs and benefits of the rule," *id.* at 1148–49, focusing exclusively on the supposed (and ill-defined) savings to PVABs while ignoring relevant costs to companies and shareholders.

Fourth, the Commission ignored its duty to consider reasonable alternatives "within the ambit of existing [policy,]" that would avoid unnecessary regulatory instability. *Dep't of Homeland Sec.* v. *Regents of the Univ. of Cal.*, 140 S. Ct. 1891, 1913 (2020) (alteration in original). The Commission failed to provide any explanation for rejecting a viable alternative to wholesale reversal—namely, conducting a retrospective review of the 2020 Rule after three to five years—suggested by various commenters and a dissenting commissioner. *Chamber of Com. of U.S.* v. *SEC*, 412 F.3d 133, 145 (D.C. Cir. 2005) (rule was arbitrary and capricious because Commission failed to consider alternatives from commenters and dissenting commissioner).

Fifth, the 2022 Rule is arbitrary and capricious because it contains "[u]nexplained inconsistenc[ies]" given the Commission's choice to defer to PVABs' self-regulation while

treating similarly situated stakeholders in the proxy process differently. *Nat'l Cable & Telecomm. Ass'n* v. *Brand X Internet Servs.*, 545 U.S. 967, 981 (2005).

For any of these reasons, this Court should set aside the 2022 Rule and the Commission's non-enforcement of the 2020 Rule, and order the Commission to reinstate the 2020 Rule and the 2020 Guidance pending any further rulemaking.

BACKGROUND

A. PVABs Develop an Enormous Influence Over Corporate Decisionmaking.

The United States has long maintained a system of shareholder democracy under which shareholders of publicly traded companies retain the right to vote on critical corporate governance decisions, such as director elections, mergers, acquisitions, executive compensation, corporate direction, and various disclosures. This voting power, however, has come to be largely exercised "by proxy," that is, through proxy-card ballots cast on behalf of shareholders, rather than votes cast in person at the shareholder meeting. Ex. 1 at 66,5198–19 (*Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice Release*, 84 Fed. Reg. 66,518, (Dec. 4, 2019)) (Proposed 2020 Rule). And in our modern financial system, around three-quarters of shares are owned not by individual "retail" investors but instead by large institutional investors, such as mutual funds or pension funds. *Id.* at 66,519. Those institutional investors vote on thousands of proposals relating to hundreds of public companies each year, with most of that voting occurring during a period of a few months known as "Proxy Season." Ex. 2 at 55,083 (*Exemptions from the Proxy Rules for Proxy Voting Advice*, 85 Fed. Reg. 55,082, (Sept. 3, 2020)) (2020 Rule).[1]

[1] *See* Fed. R. Evid. 201(b)(2) (permitting judicial notice of facts that "can be accurately and readily determined from sources whose accuracy cannot reasonably be questioned").

Without the time and personnel to thoroughly analyze each proxy voting decision, institutional investors have turned to PVABs for recommendations as to how to vote their shares. This business of providing proxy advice to institutional investors is dominated by just two firms, Institutional Shareholder Services (ISS) and Glass Lewis, which together control over 90% of the market. Ex. 2 at 55,127 n.517 (2020 Rule).

Several developments have spurred the rise of PVABs' control over the proxy voting process. Most notably, the number of issues put up for a vote has proliferated in recent years with the rise of shareholder proposals on environment, social, and governance issues (ESG), leading to investors outsourcing more of their analysis of such proposals to PVABs. *See* Ex. 3 (Freshfields, *Trends and Updates From the 2022 Proxy Season*) ("There was a record-breaking number of shareholder proposals for Russell 3000 companies, mostly related to ESG."). Many institutional investors also utilize so-called "robo-voting" procedures whereby PVABs automatically submit those institutions' votes in line with the PVABs' recommendations, without any review. AR-23/Ex. 5 at 54 (Profs. Rose & Walker Comment). Robo-voting, along with a similar practice whereby PVABs pre-populate voting forms for institutional investors to cast, predictably results in those investors voting in lock-step with PVAB recommendations. *Id*. at 59 (175 entities representing over $5 trillion in assets voted in line with ISS recommendations 95% of the time).

Because PVABs both influence and even cast a substantial number of shareholder votes, they "play the role of quasi-regulator, whereby boards feel compelled to make decisions in line with proxy advisors' policies due to their impact on voting." Ex. 49 (Doyle, *The Realities of Robo-Voting*). Thus, regulators, jurists, and scholars agree that "the effectiveness of shareholder democracy hinges on the quality of proxy advice." Ex. 6 at 25 (Matsusaka & Shu, *Does Proxy*

Advice Allow Funds to Cast Informed Votes?); Ex. 2 at 55,083 (2020 Rule) ("[P]roxy voting advice businesses have become uniquely situated in today's market to influence . . . investors' voting decisions."); Ex. 7 (Leo E. Strine, Jr., *The Delaware Way*) (explaining that it is commonplace for "powerful CEOs to come on bended knee . . . to persuade the managers of ISS of the merits of their views").

B. In the Absence of Regulation, Troubling Practices Emerge Among PVABs.

Despite their extraordinary influence on corporate governance, for decades PVABs enjoyed freedom from regulatory oversight, unlike their investment adviser clients or the heavily regulated companies that form the subject of their recommendations. All other actors engaged in proxy solicitations—*i.e.*, written communications explaining or advocating for positions on issues to be voted on at a shareholder meeting—were and are subject to stringent federal proxy rules, pursuant to which they must disclose specific information in a "definitive proxy statement" filed with the Commission. 17 C.F.R. § 240.14a-6. Because PVABs were exempt from these requirements, shareholder democracy in the United States developed into a system whereby two behemoth firms could effectively dictate the outcome of votes on critical corporate-governance topics with almost no regulatory oversight.

As PVABs' power continued to grow, several troubling issues emerged about their recommendations. First, it became clear that the various services offered by PVABs necessarily generated undisclosed conflicts of interests. As the Commission explained, some PVABs (including ISS) earn fees from providing corporate-governance consulting services to some of the same companies on which they also issue proxy voting recommendations. Ex. 1 at 66,525 (Proposed 2020 Rule). That evident conflict may lead to PVAB recommendations adverse to companies that do not purchase the PVAB's services, or force companies to "purchase consulting services from the proxy advisory firm in an effort to garner the [PVAB's] support for

the issuer when the voting recommendations are made." Ex. 50 at 43,012 (*Concept Release on the U.S. Proxy System; Proposed Rule*, 75 Fed. Reg. 42,982 (July 22, 2010)).

Second, it became clear that PVABs were basing many of their recommendations on inaccurate or incomplete information. For example, surveys conducted by the American Council for Capital Formation found that businesses were forced to file supplemental proxy materials with the Commission to dispute or correct errors contained within PVAB reports on at least 42 occasions in 2020 and 50 occasions in 2021. Ex. 8 at 9 (Am. Council for Capital Formation, *Proxy Advisors Are Still a Problem*). Those studies vastly understate the problem, because they only capture instances where companies were able to file supplemental proxy materials *before* the shareholder vote, which is often impossible to do because most PVAB recommendations are issued just days before the vote in question. For example, surveys of CEOs conducted by Plaintiff Business Roundtable in 2013 and 2018 revealed that *nearly every single respondent* had identified factual errors in PVAB recommendations. Ex. 52 (Bus. Roundtable, Comment).

Even in the rare case where a company had time to review PVAB recommendations and file supplemental proxy materials with the Commission, there was no mechanism for ensuring that shareholders were aware of, or had access to, these supplemental filings before casting their votes. Ex. 1 at 66,520, 66,533 (Proposed 2020 Rule). PVABs were under no obligation to inform their clients of these supplemental filings and they were generally unresponsive to corporate calls to do so. *Id.* at 66,520. As a result, institutions continued casting their proxy votes based on faulty and/or incomplete information, and there were no means for companies to engage in an effective dialogue with shareholders about PVAB recommendations.

Concerns about undisclosed PVAB conflicts and inaccuracies in PVAB recommendations are not academic. These issues generate substantial (and detrimental) real-

world consequences for shareholder value. Ex. 9 at 32 (Tao Li, *Outsourcing Corporate Governance: Conflicts of Interest Within the Proxy Advisory Industry*) (empirical study finding that "biased [PVAB] recommendations have real negative consequences"); Ex. 10 at 8, 13 (NAM *Outlook Survey*) (over half of public companies surveyed reported diverting resources from their core business functions in attempting to respond to PVAB recommendations).

C. The Commission Embarks on a Decade-Long Effort to Craft Appropriate Regulations for PVABs, Culminating in the 2020 Rule.

Recognizing these problems, beginning in 2010, the Commission began investigating the risks PVABs posed to publicly traded companies and their shareholders. *See* Ex. 11 (Chairman Schapiro, *Opening Statement at the SEC Open Meeting* (July 14, 2010)) (detailing concept release to investigate PVABs' "undisclosed conflicts of interest," "fail[ure] to conduct adequate research" and "recommendations [based] on erroneous or incomplete facts"). The Commission's decade-long, bipartisan process involved multiple requests for public input and fact-finding discussions. *See* Ex. 12 (Release No. 34–86721, *Commission Interpretation and Guidance*, 84 Fed. Reg. 47,416 (Sept. 10, 2019)) (detailing requests for public comment in 2010, 2013, and 2018, as well as roundtable discussions held in 2013 and 2018).

On December 4, 2019, this extensive process culminated with the Commission's issuance of a Proposed Notice of Rulemaking. The Commission reiterated its "concern[] about the risk of [PVABs] providing inaccurate or incomplete voting advice . . . that could be relied upon to the detriment of investors." Ex. 1 at 66,520 (Proposed 2020 Rule). Moreover, registrants had expressed that they lacked "meaningful opportunities to engage" with PVABs to address any errors or methodological weaknesses. *Id.* at 66,529. The Commission therefore proposed "amendments to the federal proxy rules" designed "to enhance the accuracy, transparency of process, and material completeness of the information provided to clients of [PVABs]." *Id*. at

66,520. During the 60-day comment period that followed, 650 comments were submitted by members of the public, and the Commission staff engaged in 84 meetings with interested parties. Ex. 42 (*Comments on Proposed Rule: Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice*, Release No. 34-8757; File No. S7-22-19).

The 2020 Rule was formally issued on September 3, 2020. It amended the Commission's proxy rules to clarify that the issuance of proxy voting advice by PVABs constitutes a solicitation under the securities laws. Accordingly, like all other actors who disseminate information in the proxy voting process, PVABs are subject to the proxy rules. Ex. 2 at 55,084 (2020 Rule). The 2020 Rule, however, also created several conditions that, if met, would exempt PVABs from the proxy rules' information and filing requirements. First, PVABs were required to disclose any potential conflicts of interests. *Id.* at 55,154. Second, PVABs were required to adopt policies designed to reasonably ensure that "[r]egistrants that are the subject of the proxy voting advice have such advice made available to them at or prior to the time when such advice is disseminated to the [PVAB's] clients," and to "provide[] [their] clients with a mechanism by which they can reasonably be expected to become aware of any written statements regarding its proxy voting advice by registrants who are the subject of such advice, in a timely manner." *Id.* (Review and Notice Conditions).

The 2020 Rule reflected notable substantive revisions from the Proposed 2020 Rule in response to public comments and meetings. For example, while the Proposed 2020 Rule would have required PVABs to provide *draft* recommendations to registrants before they were provided to the PVABs' clients, the final 2020 Rule required only that PVABs make available their recommendations to registrants at the same time that they distributed their final recommendations to their clients. *Id.* at 55,109–11. This change responded to concerns raised

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by PVABs and some investors that any advance review requirement could impact the cost, timeliness, and independence of PVAB recommendations.

The 2020 Rule also made clear that PVABs are subject to the antifraud provisions that govern proxy solicitations. *Id.* at 55,155. By adding Note (e) to the antifraud regulations, the Commission clarified that the "[f]ailure to disclose material information regarding proxy voting advice . . . such as the [PVAB's] methodology, sources of information, or conflicts of interest" may constitute a misstatement. *Id*. Finally, the Commission issued the 2020 Guidance alongside the 2020 Rule to encourage investment advisers to disclose their policies and procedures relating to robo-voting. This guidance was aimed at ensuring that investment advisers' clients are "able to understand the role of automated voting in the investment adviser's exercise of voting authority." Ex. 13 at 55,156 (*Supplement to Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers*, 85 Fed. Reg. 55,155 (Sept. 3, 2020)).

The Final Rule was "overwhelmingly supported" by public companies and retail investors. AR-42/Ex. 15 (Nasdaq, Comment) (citing survey revealing that 99% of public companies and 81% of retail investors aware of the Rule supported it). Despite the quite modest nature of the 2020 Rule's reforms, PVABs refused to accept *any* regulation, and promptly sued the Commission to set aside the 2020 Rule. *See ISS Inc.* v. *SEC*, No. 19-cv-3275 (D.D.C. 2020).

D. The New Commission Majority Effectively Rescinds the 2020 Rule Through a Policy of Non-Implementation and Non-Enforcement.

The 2020 Rule provided PVABs until December 1, 2021—more than 14 months—to implement policies in compliance with it. Ex. 2 at 55,122 (2020 Rule). Yet six months before that date, on June 1, 2021, a new majority of Commissioners sent a clear message—through coordinated, irregular, and unlawful actions—that they intended to rescind the 2020 Rule.

First, new Commission Chairman Gensler released a statement directing the staff to "consider whether to recommend that the Commission revisit" the 2020 Rule. Ex. 16 (Chairman Gensler, *Statement on the Application of the Proxy Rules to Proxy Voting Advice* (June 1, 2021)). Later that same day, the Commission's Division of Corporation Finance issued a statement of its own, declaring that it would not recommend enforcement action based on the 2020 Rule while the Commission considered "further regulatory action in this area." Ex. 14 (*Statement on Compliance with the Commission's 2019 Interpretation and Guidance* (June 1, 2021)).[2] Tipping its hand even more as to its inevitable course, the Commission filed a motion to hold in abeyance ISS's legal challenge to the 2020 Rule, pending the Commission's reconsideration of the 2020 Rule. *ISS Inc.* v. *SEC*, No. 19-cv-3275, Dkt. 53 at 4 (D.D.C. June 1, 2021). The motion stated that PVABs would no longer have to comply with the upcoming deadline for the 2020 Rule. *Id.*

Second, ten days later, on June 11, 2021, Chairman Gensler and members of the Commission staff held a closed-door meeting with 21 representatives from large institutional investors and affiliated industry groups who had *all* opposed the 2020 Rule. According to a footnote in the Proposed 2022 Rule—the only disclosure the Commission has made regarding the substance of this closed-door meeting—the attendees used this private meeting to express their continued opposition to the 2020 Rule. Ex. 17 at 67,385 n.24 (*Proxy Voting Advice,* 86 Fed. Reg. 67,383 (Nov. 26, 2021)) (Proposed 2022 Rule). Although the Commission published a two-page memorandum listing the meeting attendees, the memorandum only referenced a discussion of a separate rule proposal regarding universal proxy cards, and curiously left out any

[2] The Commission's refusal to enforce the 2020 Rule was challenged under the APA for contravening the requirement that an agency engage in notice-and-comment rulemaking when it rescinds a regulation. *See Nat'l Assoc. of Mfrs.* v. *SEC*, No. 21-cv-183 (W.D. Tex. 2021).

mention of the 2020 Rule. Nor has the Commission yet responded to Plaintiff U.S. Chamber's FOIA requests on this issue, which have now been pending for eight months.

E. The Commission Formally Reverses the 2020 Rule by Promulgating the 2022 Rule on an Artificially Truncated Timeline.

1. The Proposed 2022 Rule

On November 26, 2021, before the 2020 Rule had even gone into effect, the Commission issued a new proposed rule on proxy voting advice. The Proposed 2022 Rule would have rescinded the 2020 Rule's Review and Notice Conditions. To escape the burdens of the federal proxy rules, PVABs would no longer need to adopt written policies and procedures reasonably designed to (1) allow registrants that are the subject of voting advice to access that advice at the same time as PVABs circulated the advice to clients, or (2) provide PVABs' clients with a timely notification of registrants' responses to PVABs' recommendations. Ex. 17 at 67,385-86 (Proposed 2022 Rule). The Proposed 2022 Rule also deleted Note (e), which contained examples of possible misstatements in proxy voting advice. *Id.* at 67,390.

The two justifications for the Proposed 2022 Rule, which was issued by a 3-2 party-line vote, were the continuing "strong concerns" of certain investors regarding the 2020 Rule's potential impact on the "independence, cost, and timeliness" of proxy voting advice and the development of voluntary "best practices" by the PVAB industry. *Id.* at 67,384, 67,291. But both of these points had been raised by PVABs and addressed by the Commission when formulating the 2020 Rule. Dissenting Commissioners highlighted the absurdity of promulgating a new rule based on concerns that the Commission had addressed just a few months earlier, with Commissioner Peirce stating that while "[t]he release takes a stab at justifying the rewrite . . . we might as well simply acknowledge that the political winds have shifted." Ex. 18 (Commissioner Peirce, *Dissenting Statement*).

The Commission's Proposed 2022 Rule was issued with an inadequate 30-day comment period—from November 27 to December 27, 2021—which overlapped with several year-end holidays and fiscal deadlines for many public companies, leaving key stakeholders with little time to weigh in. An easy solution would have been to extend the comment period, which several commenters requested. *See* Ex. 19 (U.S. Chamber of Commerce, Comment); Ex. 20 (Am. Sec. Ass'n, Comment). The Commission ignored those requests. Unsurprisingly, the Commission received just 61 comments during the rushed comment period—fewer than one-tenth of the 650 comments received in response to the 2020 Rule. Ex. 48.

2. The 2022 Rule

On July 13, 2022, the Commission approved the 2022 Rule by another 3-2 party-line vote. Unlike the 2020 Rule, which thoughtfully incorporated public feedback through significant revisions to the Proposed 2020 Rule, the substance of the 2022 Rule remained entirely unchanged from the Proposed 2022 Rule.

That same day, the Commission issued a proposed rule limiting certain bases for excluding shareholder proposals from proxy cards. *See* Ex. 4 (*Substantial Implementation, Duplication, and Resubmission of Shareholder Proposals Under Exchange Act Rule 14a-8*, SEC Release 87 Fed. Reg. 45,052 (July 27, 2022)) (Shareholder Proposal Rule). Thus, at the same time that the Commission reduced companies' abilities to effectively respond to PVAB recommendations, it took steps to ensure that there will be *more* proposals put up for vote, which will in turn engender *more* reliance on PVABs' recommendations. The 2022 Rule did not even consider the implications—or the costs—of these interconnected rules.

The Commission attempted to justify its reversal of the Review and Notice Conditions by relying on the same two rationales as in the Proposed 2022 Rule. Specifically, the Commission cited "*continued*, strong opposition to the [Review and Notice Conditions] from many

institutional investors and other PVAB clients . . . who have *continued* to raise concerns that the [Review and Notice Conditions] would have adverse effects on the cost, timeliness, and independence of proxy voting advice," and that the Review and Notice Conditions were unnecessary due to voluntary self-regulation by PVABs. Ex. 21 at 43,170 (2022 Rule) (emphasis added). In reviving concerns that had already been considered and addressed in the 2020 Rule, the Commission failed to identify *any* facts (much less new ones) to substantiate the notion that requiring PVABs to provide a copy of their final recommendations to a registrant at the same time as providing them to their clients would have adverse effects on the cost, timeliness, or independence of PVABs' advice. Nor did it suggest why voluntary industry practices previously rejected as inadequate now obviated the need for regulation. *Id.* at 43,176.

The 2022 Rule also removed Note (e), which provided examples of what could constitute misleading information in proxy voting advice under the federal proxy rules' antifraud provisions. Without citing any evidence, the 2022 Rule asserted that these examples could lead to "a risk of confusion" and "heightened legal uncertainty" for PVABs. *Id.* at 43,180-43,181. This unsupported proposition was directly contradicted by the Commission's own findings in the 2020 Rule that it "d[id] not expect the new amendment to Rule 14a-9 to generate significant new litigation risk." Ex. 2 at 55,140 (2020 Rule). And the Commission itself "risked confusion" by eliminating Note (e) while simultaneously asserting that the rescission did "not affect the scope of Rule 14a-9 or its application to proxy voting advice," and reiterating the language of Note (e) verbatim as the current governing standard in the Release to the 2022 Rule. Ex. 21 at 43,180 (2022 Rule).

Finally, the 2022 Rule rescinded the common-sense 2020 Guidance that accompanied the 2020 Rule calling on investment advisers to evaluate and disclose their policies regarding their

use of robo-voting. *Id*. at 43,168. In doing so, the Commission ignored numerous concerns expressed about investment advisers' overreliance on robo-voting systems.[3]

LEGAL STANDARD

A court's "review of a final agency determination under the APA" is typically resolved at summary judgment because "resolution of the matter does not require fact finding on behalf of [the] court." *Harkness* v. *Sec'y of the Navy*, 174 F. Supp. 3d 990, 1004 (W.D. Tenn. 2016) (quotation and alterations omitted). The APA "requires agencies to engage in 'reasoned decisionmaking.'" *Regents*, 140 S. Ct. at 1905 (quoting *Michigan* v. *EPA*, 576 U.S. 743, 750 (2015)). And it directs that agency actions be 'set aside' if they are 'arbitrary' or 'capricious.'" *Id.* (quoting 5 U.S.C. § 706(2)(A)). Where, as here, an agency "chang[es] position," its action is subject to additional constraints. *FCC* v. *Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009). It must "show that there are good reasons for the new policy" and, when the "new policy rests upon factual findings that contradict those which underlay [a] prior policy" it must provide a "more detailed justification than what would suffice for a new policy created on a blank slate." *Id*. "[A]n unexplained inconsistency in agency policy is a reason for holding an interpretation to be an arbitrary and capricious change from agency practice." *Brand X Internet Servs.*, 545 U.S.

[3] Plaintiffs standing to challenge the 2022 Rule is self-evident. Plaintiffs' members have incurred and will continue to incur economic injuries from the Commission's rescission of the 2020 Rule because they incur numerous costs in scrambling to respond to inaccuracies and incomplete information in PVABs' recommendations—harms that the 2020 Rule was intended to ameliorate. Compl. ¶¶ 35-39, 55-59. A favorable decision would redress those injuries by restoring policies that would require Plaintiffs' members to expend far fewer resources when attempting to discover and issue responses to PVAB advice before a shareholder vote. *Id*. And because the 2022 Rule deprives Plaintiffs' members of the opportunity to review and respond to PVAB recommendations in a timely manner, proxy voting decisions will be made based on inaccurate or incomplete information, which further harms member companies and their shareholders. *Id*. ¶ 35. Finally, the rescission of Note (e) creates regulatory uncertainty and harms Plaintiffs because they may no longer be able to rely on the examples set forth in Note (e) to hold PVABs legally accountable.

at 981. Finally, "[w]hen an agency rescinds a prior policy its reasoned analysis must consider the alternatives that are within the ambit of the existing policy." *Regents*, 140 S. Ct. at 1913.

ARGUMENT

I. THE COMMISSION'S INADEQUATE PROCESS VIOLATED THE APA (COUNT I).

As a threshold matter, the Commission violated the APA in promulgating the 2022 Rule, because the Commission did not "give interested persons an opportunity to participate in the rulemaking through submission of written data, views, or arguments." 5 U.S.C. § 553(c). Courts have consistently made clear that the "opportunity for comment" must be "a meaningful opportunity." *Rural Cellular Ass'n*, 588 F.3d at 1101; *see N. Carolina Growers' Ass'n, Inc.* v. *United Farm Workers*, 702 F.3d 755, 763 (4th Cir. 2012) (same); *Prometheus Radio Project* v. *FCC,* 652 F.3d 431, 450 (3d Cir. 2011) (same). The requirement is not a mere formality; it is meant to ensure that the public has "enough time with enough information to comment," *id*., 652 F.3d at 451, and that the agency "maintains a flexible and open-minded attitude towards its own rules," *N. Carolina Growers'*, 760 F.3d at 763 (quotation omitted). Accordingly, courts have repeatedly vacated rules based on comment periods of insufficient length. *See*, *e.g.*, *Prometheus*, 652 F.3d at 453 (28-day comment period rather than "usual 90 days" was arbitrary and capricious); *Becerra* v. *U.S. Dep't of the Interior*, 381 F. Supp. 3d 1153, 1177 (N.D. Cal. 2019) (30-day comment period was arbitrary and capricious); *Cath. Legal Immigr. Network, Inc*. v. *Exec. Off. for Immigr. Rev.*, 2021 WL 3609986, at *3 (D.D.C. Apr. 4, 2021) (30-day comment period was inadequate and violated Executive Branch policy of providing 60 days for comment).

To assess how much time would be "enough," "in cases involving the repeal of regulations, courts have considered the length of the comment period utilized in the prior rulemaking process." *Becerra*, 381 F. Supp. 3d at 1177 (30-day comment period for the repeal

of rule created following a 120-day comment period was inadequate). Here, the 60-day comment period provided for the 2020 Rule, combined with the complexity of the rulemaking and importance of the subject matter, established the need for a comment period longer than 30 days to allow for meaningful public feedback. *See Est. of Smith* v. *Bowen*, 656 F. Supp. 1093, 1098-99 (D. Colo. 1987) (finding rule to be "invalid" because the 60-day comment period was insufficient in light of the "great numbers of interested persons" and because organizations could not reasonably comment in 60 days).

Critically, this already too-short comment period was further compressed because it ran from November 27, 2021 (the Friday after Thanksgiving) to December 27, 2021 (the Monday after Christmas), and thus conflicted with the year-end holidays, including Christmas, Hanukkah, and Kwanzaa. *See Pangea Leg. Servs.* v. *U.S. Dep't. of Homeland Sec*., 501 F. Supp. 3d 792, 820 (N.D. Cal. 2020) (30-day comment period that "span[ned] the holidays" was inadequate in light of importance of subject matter and magnitude of rule, particularly compared to comment periods for similar rules). And the truncated comment period also coincided with the busy year-end fiscal deadlines for many public companies. As a result, many interested parties did not have the time or resources to dedicate to public comment.

To make matters worse, the Commission entirely ignored commenter requests to extend the comment period—despite granting such extensions in contemporaneous rulemakings. *See e.g.,* Ex. 22 (*SEC Extends Comment Period for Proposed Rules on Climate-Related Disclosures, Reopens Comment Periods for Proposed Rules Regarding Private Fund Advisers and Regulation ATS*, (May 9, 2022)) ("The SEC benefits greatly from hearing from the public.").[4]

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[4] The Commission also held just four meetings with limited participants in which it discussed the 2022 Rule. *See* AR-63/Ex. 23, AR-64/Ex. 24, AR-65/Ex. 25 (Meeting

The rushed 30-day comment period also conflicted with prior administrative practice. The Executive Branch has repeatedly recognized that "a meaningful opportunity to comment . . . should include a comment period of not less than 60 days." Ex. 26 (Exec. Order No. 12866) (Clinton Administration); Ex. 27 (Exec. Order 13258) (Bush Administration); Ex. 28 (Exec. Order No. 13563) (Obama Administration); Ex. 29 (Memorandum for the Heads of Executive Departments and Agencies, *Modernizing Regulatory Review*, 86 Fed. Reg. 7223 (Jan. 20, 2021)) (Biden Administration). The Administrative Conference of the United States, an independent federal agency designed to improve agency processes and procedures similarly recommends not fewer than 60 days for public comment. *See* Ex. 30 (Administrative Conference of the United States, Rulemaking Comments, Recommendation No. 2011-2 (June 16, 2011)). Indeed, in the words of Chairman Gensler, the Commission has a professed policy that market participants will "always" receive "at least two months" to comment on Commission rule proposals. Ex. 31 at 7 (House Appropriations Subcom. on Fin. Servs, *Hearing on the Fiscal Year 2023 SEC and Federal Trade Commission Budget Request* (May 18, 2022)). It is "troubling that defendants failed to abide by these guidelines or explain their departure from them." *Cath. Legal Immigr. Network,* 2021 WL 3609986, at *3 (insufficient comment period in violation of executive order guidelines was arbitrary and capricious).

The inadequacy of the Commission's comment period is "borne out" by the administrative record: the 2022 Rule received a paltry 61 comments compared to 650 comments for the 2020 Rule. *Pangea Legal Servs.*, 501 F. Supp. 3d at 820 ("insufficiency of notice process" reflected in repeal receiving "far fewer comments"). As one of the dissenting

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Memoranda); Ex. 17 at 67,385 n.24 (Proposed 2022 Rule). That stands in stark contrast to the *84 meetings* held with the public in connection with the 2020 Rule.

Commissioners recognized, the truncated comment period "likely deterred some interested persons from submitting comment letters" and "may have also resulted in the Commission only seeing a narrower picture of the public concerns." Ex. 32 (Commissioner Uyeda, *Statement on Final Rule Amendments on Proxy Voting Advice* (July 13, 2022)).

In sum, the 30-day comment period (spanning the holidays and year-end financial reporting period) was shorter than the comment period utilized during the 2020 rulemaking, violated the Commission's own policy of providing "at least" 60 days to comment, and contravened the 60-day comment period endorsed by prior Administrations and the Administrative Conference. The truncated comment period (coupled with the extremely limited public meetings) deprived interested parties of a meaningful opportunity to participate in the Commission's rulemaking. On that basis alone, this Court should set aside the 2022 Rule.

II. THE COMMISSION'S ARBITRARY AND CAPRICIOUS REVERSAL OF THE 2020 RULE VIOLATED THE APA (COUNTS II-VI).

Unsurprisingly, after failing to engage meaningfully with the public and forging ahead with its predetermined policy, the Commission promulgated a poorly informed rule that does not satisfy its substantive obligations under the APA.

A. The Commission Failed to Give a Rational Explanation for Reversing Course When the Factual Record Was Unchanged (Counts III and IV).

The 2020 Rule embodied the Commission's reasoned determination that modest regulation of PVABs was warranted to facilitate more transparent and accurate information for shareholders to make their proxy voting decisions. The Supreme Court has made clear in recent years that the APA demands more of an agency when it is "chang[ing] course." *Regents*, 140 S. Ct. at 1913 (setting aside agency policy reversal as arbitrary and capricious). Although "a summary discussion may suffice in *other* circumstances," when an agency reverses itself it must "explain why it deemed it *necessary* to overrule its previous position." *Encino Motorcars,* 579

U.S. at 222 (emphasis added) (regulation was arbitrary and capricious because agency failed to adequately explain reversing itself). And when a "new policy rests upon factual findings that contradict those which underlay [an agency's] prior policy," the agency must "provide a more detailed justification than what would suffice for a new policy created on a blank slate." *Fox Television*, 556 U.S. at 515. Here, the Commission never explained—much less provided a *more detailed* explanation—why the *same* facts and circumstances that supported the 2020 Rule could be almost immediately ignored. Instead, the Commission offered up "summary" justifications for its reversal, which do not "suffice." *Encino Motorcars*, 579 U.S. at 222.

First, the Commission claimed that "many investors and PVAB clients have *continued* to raise concerns that the [Review and Notice Conditions]" will have "adverse effects on the cost, timeliness, and independence of proxy voting advice." Ex. 21 at 43,170 (2022 Rule) (emphasis added). But these exact concerns were raised and addressed during the 2020 rulemaking process. *See* Ex. 2 at 55,112 (2020 Rule) ("We believe we have addressed the concerns raised by commenters . . . related to timing and the risk of affecting the independence of the advice."); *id.* (commenters' concerns "regarding increased marginal costs . . . should be alleviated"). Specifically, the Commission removed the requirement that PVABs give companies an advance review of their advice in *draft* form, opting instead to require PVABs only to provide their *final* advice to companies at the same time as they provide it to their clients. With this change, the Commission concluded that "the rule does not create the risk that [PVAB] advice would be delayed or that the independence thereof would be tainted as a result of a registrant's pre-dissemination involvement." *Id*. As Commissioner Peirce observed with respect to the 2022 Rule, the comment letters that the Commission cited "did not include new information to justify the Commission's U-Turn. Instead, they reiterated concerns that commenters had raised during

the prior rulemaking process." Ex. 33 (Commissioner Pierce, *U-Turn, Comments on Proxy Voting Advice*). In fact, the majority of comments on the Proposed 2022 Rule favored "the Commission leaving intact its 2020 work." *Id*.

Rather than provide a reasoned explanation for why the 2020 Rule still threatened the cost, timeliness, and independence of PVABs' advice, the Commission simply asserted that it was "weigh[ing] competing concerns differently today." Ex. 21 at 43,175 (2022 Rule). That is precisely the sort of baseless "summary discussion" that falls "short of the agency's duty to explain why it deemed it necessary to overrule its previous position." *Encino Motorcars*, 579 U.S. at 222. Critically, the Commission did not point to any evidence—new or old—or changed circumstances to justify *why* concerns that were raised two years ago should be weighed differently today. In other words, the agency failed to supply "good reasons" for the change-in-position, a fatal flaw in its analysis that renders the rule arbitrary and capricious. *Organized Vill. of Kake* v. *USDA*, 795 F.3d 956, 967 (9th Cir. 2015) (failure to explain change in position within a two-year period rendered rule arbitrary and capricious).

At bottom, the Commission simply asserted that the 2020 Rule could harm the cost, timeliness, or independence of PVAB advice. The Commission did not say that the 2020 Rule would have those effects—and the Commission never explained how or why it would. *United Mine Workers of Am.* v. *Mine Safety & Health Admin.*, 626 F.3d 84, 94 (D.C. Cir. 2010) (conclusory reasoning basis for setting aside rule as arbitrary and capricious). Because agencies must "critically review[]" analysis provided by interested parties or perform their own analysis to support factual claims, blindly embracing parties' self-serving comments does not meet the Commission's obligations under the APA. *Susquehanna Int'l Grp.* v. *SEC*, 866 F.3d 442, 447 (D.C. Cir. 2017) (acceptance of interested parties' comments without making "an independent

review" was arbitrary and capricious); *Greene Cnty. Planning Bd.* v. *Fed. Power Comm'n*, 455 F.2d 412, 420–22 (2d Cir. 1972) (invalidating action where agency "substitut[ed] the statement of [the regulated entity] for its own" due to "the potential, if not likelihood, that the [regulated entity's] statement will be based upon self-serving assumptions").

Second, the Commission sought to justify its rule reversal on the basis that "certain voluntary practices of PVABs . . . are likely, at least to some extent, to advance the goals underlying the [Review and Notice Conditions]." Ex. 21 at 43,170 (2022 Rule). Once again, the Commission had already considered industry self-regulation in promulgating the 2020 Rule and concluded that "we do not believe the existing voluntary forms of outreach to registrants and other market participants . . . are alone sufficient." Ex. 2 at 55,108 (2020 Rule). In particular, the Commission concluded in 2020 that those voluntary programs were not comprehensive, complete, or universally followed, and PVABs could choose to abandon those industry standards at any time. *Id.* at 55,108. Less than two years later, the Commission failed to cite any evidence or change in circumstances to support reaching the opposite conclusion about self-regulation. And the Commission could only bring itself to say that self-regulation would likely aid transparency "at least to some extent"—hardly a ringing endorsement of self-policing.

The Commission's reasoning would not have sufficed even if it had been writing on a "blank slate." *Fox Television*, 556 U.S. at 515. That is so because the Commission's reliance on PVAB self-regulation "run[s] counter to the evidence before the agency." *Nat'l Ass'n of Home Builders* v. *Defs. of Wildlife*, 551 U.S. 644, 658 (2007). As the Commission acknowledged, the largest PVAB, ISS, had changed its policies in January 2021 in a way that *reduced* engagement with issuers by eliminating any opportunity for companies to provide feedback on ISS's draft voting recommendations. Ex. 17 at 67,389 n.59 (Proposed 2022 Rule). Furthermore, the

Commission noted that "[ISS] does not allow registrants to share [PVAB] advice with any external parties" such as its attorneys, proxy solicitors, or compensation consultants, which "may inhibit a registrant's ability to adequately respond . . . in a manner that would benefit its shareholders." *Id*. at 67,387 n.59. And while the Commission pointed to Glass Lewis's implementation of a "Feedback Service," which would allow select companies to offer comments on Glass Lewis's voting recommendations, Ex. 21 at 43,172 (2022 Rule), the Commission declined to address comments expressing frustration with that service on the ground that it is expensive and only intermittently made available. AR-42/Ex O (Nasdaq, Comment). The Commission's deference to voluntary industry standards amounts to nothing more than blindly "[t]rusting the process" of self-regulation, which "is simply not enough" under the APA. *Susquehanna Int'l Grp*., 866 F.3d at 449.

Separate from rescinding the Review and Notice Conditions, the Commission's purported rationales for removing Note (e) to the SEC's antifraud rule, Rule 14a-9, and for rescinding the 2020 Guidance concerning robo-voting, are insufficient under the APA. As it had done in abandoning the Review and Notice Conditions, in eliminating Note (e), the Commission merely cited concerns that PVABs and certain institutional investors had previously raised during the 2020 rulemaking—namely, a purported "risk of confusion regarding the application of Rule 14a-9 to proxy voting advice" and "heightened legal uncertainty" for PVABs. Ex. 21 at 43,170, 43,180 (2022 Rule). As the Commission had then explained, Note (e) did not heighten any litigation risk because it merely reinforced prior guidance and "clarifie[d] what has long been true about the application of Rule 14a-9 to proxy voting advice." Ex. 2 at 55,121 (2020 Rule).

The Commission failed to offer an explanation as to how a "clarification" of PVABs' obligations under the antifraud rule could somehow confuse or heighten legal *uncertainty*.

Moreover, despite removing Note (e)'s illustrative examples, the Commission perplexingly stated that doing so was not intended to change the liability standard. Ex. 21 at 43,181 (2022 Rule). And even more inexplicably, the Commission included the entirety of the now-eliminated Note (e) in the 2022 Rule Release as an explanation of the liability standard. *Id.* at 43,180. Rather than reducing confusion about the liability standard, the Commission's decision to eliminate Note (e) has only increased it.

Similarly, the Commission acted arbitrarily by rescinding its common-sense 2020 Guidance about robo-voting. The 2020 Guidance urged investment advisers to disclose the extent and circumstances in which they use robo-voting and to evaluate how those policies could accommodate subject companies' responses to PVAB recommendations. In rescinding the 2020 Guidance, the Commission stated that it was no longer necessary given the 2022 Rule's repeal of the Review and Notice Conditions. Ex. 21 at 43,178 (2022 Rule). That is not logical. As numerous commenters on the Proposed 2022 Rule explained, institutional investors' and investment advisers' "overreliance" on these automated voting systems makes incorporating issuer responses nearly impossible. AR-14/Ex. 34 (Prof. Li, Comment). In the absence of the 2020 Rule's Review and Notice Conditions, the need for investment advisers that use robo-voting to disclose that practice to their clients is *more* important, not less.

B. The Commission Failed to Engage in a Thorough Economic Analysis as Required by the Exchange Act (Count II).

The 2022 Rule also violates the APA because it fails to satisfy one of the Commission's statutory obligations. Specifically, Section 3(f) of the Exchange Act requires the Commission to perform a robust economic analysis of the market impact of any proposed rule. *See* 25 U.S.C. § 78c(f). Accordingly, courts have set aside rules when the Commission has neglected its statutory responsibility to "adequately . . . assess the economic effects of a new rule." *Bus.*

Roundtable, 647 F.3d at 1148; *Chamber of Com.*, 412 F.3d at 144 (rule was arbitrary and capricious because Commission failed to "apprise itself—and hence the public and the Congress—of the economic consequences of a proposed regulation"). In promulgating the 2022 Rule, the Commission committed a textbook violation of its obligations under the Exchange Act, conducting a cursory, inadequate economic analysis that "opportunistically framed [the 2022 Rule's] costs and benefits." *Bus. Roundtable*, 647 F.3d at 1148-49.

First, on its face, the Commission's hasty economic analysis pales in comparison to the analysis it conducted in connection with the 2020 Rule. The 2020 Rule offered an extensive study of its potential economic effects across 24 pages of the Federal Register. *See* Ex. 2 at 55,122-45 (2020 Rule). The Commission conducted a detailed analysis of the costs and benefits of the Rule, quantified those costs and benefits, and responded to problems raised by commenters. By contrast, the 2022 Rule is less than a quarter of that length and focuses entirely on the purported benefits to PVABs' profitability, while *ignoring* the significant costs to companies and shareholders. Ex. 21 at 43,183-89 (2022 Rule). Courts have admonished that when agencies are charged with conducting an economic analysis, "it is a small matter to abide by the injunction of the arithmetic teacher: Show your work!" *City of Holyoke Gas & Elec. Dep't* v. *FERC*, 954 F.2d 740, 743 (D.C. Cir. 1992). The Commission's failure to "show its work" was particularly egregious here where it was reaching the opposite conclusion on the same issues and the same facts it had considered just two years earlier.

Second, the Commission's analysis of the purported benefits of the rule reversal "contradict[ed] itself." *Bus. Roundtable*, 647 F.3d at 1149. The Commission claimed that the removal of the Review and Notice Conditions would "reduce the direct costs of satisfying [that] requirement." Ex. 21 at 43,186 (2022 Rule). But the Commission also assumed that PVABs

have certain "voluntary practices" such as "internal policies and procedures aimed at enabling feedback from certain registrants." *Id*. at 43,188, 43,196. If that is true, then the cost savings in employee hours from eliminating the requirement that PVABs notify their clients of such feedback should be small given that PVABs already track issuer feedback. "The Commission cannot have it both ways." *Gen. Chem. Corp.* v. *United States*, 817 F.2d 844, 854 (D.C. Cir. 1984) (vacating and remanding due to "an internal inconsistency in the Commission's opinion").

Third, the Commission dramatically understated the costs imposed on companies and investors by its reversal. Ample record evidence demonstrates that PVABs' recommendations often contain inaccurate or incomplete information. Ex. 2 at 55,105 (2020 Rule). When companies cannot address these deficiencies prior to the shareholder vote, that undoubtedly results in uninformed voting, which in turn diminishes shareholder value. Ex. 21 at 43,173 (2022 Rule). The Commission downplayed those costs based on its new view that the error rate in PVAB recommendations was low, citing only the ACCF study, *supra* at 7, which found that dozens of companies were forced to prepare supplemental filings to correct inaccurate or incomplete information in PVABs' advice. *Id.* at 43,187.[5] The Commission drew the perverse conclusion that the supplemental filings showed the need for less regulation, because "registrants were able to identify those issues and respond using pre-existing mechanisms." *Id.* at 43,176.

Beyond its facial implausibility, the Commission's conclusion ignored record evidence that numerous other companies lacked the time and resources to review PVABs' advice and file corrections in supplemental proxy statements prior to the shareholder vote, and that those filings

[5] The Commission's selective invocation of the record ignored abundant evidence that PVABs frequently offer voting recommendations premised on inaccurate information. *See, e.g.*, AR-5/Ex. 19 (U.S. Chamber of Commerce, Comment), AR-19/Ex. 36 (Prof. Verret, Comment), AR-30/Ex. 37 (Bus. Roundtable, Comment), AR-42/Ex. 16 (Nasdaq, Comment), AR-46/Ex. 38 (Nat. Gas Serv. Grp., Comment).

are not guaranteed to reach shareholders prior to a vote (particularly in light of robo-voting). *See, e.g.*, Ex. 35 (Exxon, Comment) ("Our experience is that supplemental proxy materials filed with the SEC after the release of the proxy advisors' reports . . . are ineffective."). The Commission also bizarrely asserted that "market . . . competitiveness" would reduce the incidence of errors in PVAB voting advice, notwithstanding its earlier acknowledgement that the PVAB industry is a duopoly. Ex. 21 at 43,187 (2022 Rule); Ex. 33 (Commissioner Pierce, *U-Turn*) ("[G]iven the concentration in the proxy voting advice market, proxy advisors have limited incentives to engage with public companies . . . and correct errors").

Whatever the frequency or magnitude of factual errors in PVAB advice—both historically and in the future—the Commission acted irrationally by disregarding the fact that there would be *some* error rate that would impose *some* costs on shareholders and companies. As one commenter explained, "when tens of thousands of proposals are voted on every year, even a small percentage of errors could have profound effect on the information that is used to cast those votes." AR-60/Ex. 39 (Bipartisan Policy Center, Comment). It follows that if companies do not have an effective means to learn of and respond in a timely fashion to incorrect or incomplete PVAB recommendations, costs to companies and shareholders will follow.

The Commission also failed to consider altogether the costs under the 2022 Rule that could accrue from PVABs acting on self-interested objectives, regardless of the error rate. As explained above, PVABs' advice can be motivated by other goals beyond increasing shareholder value, and can be premised on misunderstandings, or apparent conflicts of interest. It follows that if companies do not have a meaningful opportunity to respond to PVAB recommendations, costs to companies and shareholders will result. *Bus. Roundtable*, 647 F.3d at 1152 (finding that "investors with a special interest . . . can be expected to pursue self-interested objectives rather

than the goal of maximizing shareholder value, and will likely cause companies to incur costs," and that the SEC "acted arbitrarily" when it "duck[ed] serious evaluation of th[ose] costs"); Ex. 2 at 55,107 (2020 Rule) ("*Regardless of the incidence of errors* in proxy voting advice, we believe it is appropriate to adopt reasonable measures designed to promote the reliability and *completeness* of information available to investors.") (emphasis added). The Commission's failure to take into account these costs to companies and shareholders is another way in which it did not fulfill its statutory obligation to "adequately . . . assess the economic effects of a new rule." *Bus. Roundtable*, 647 F.3d at 1148.

C. The Commission Failed to Consider Viable Alternatives (Count V).

Under the APA, when an agency reverses itself it must do more than provide a "detailed justification" for its decision (which the Commission failed to do here). It must also guard against regulatory instability by first considering reasonable "alternatives . . . within the ambit of the existing policy." *Regents*, 140 S. Ct. at 1913 (quotation omitted). Here, the Commission did not consider viable alternatives to a wholesale rescission of the Review and Notice Conditions that were proposed by commenters and members of the Commission. Notably, Commissioner Peirce and various commenters cautioned against rescinding a rule that had never been implemented based on fears about costs, timeliness, and independence of PVABs' advice that had never been substantiated. Instead, Commissioner Peirce proposed that "[a] more reasonable approach would be to commit to a retrospective review of the 2020 Final Rules after three or five years to evaluate their effectiveness." Ex. 18 (Commissioner Peirce, *Dissenting Statement*).

Although the 2022 Rule acknowledged that commenters had proposed this alternative, the Rule failed to give it any consideration, much less provide a reasoned explanation for its rejection. Ex. 21 at 43,174 (2022 Rule). The Commission's failure in this respect was particularly glaring given that it owes a special obligation to consider an alternative proposal or

objection raised by a dissenting Commissioner when it is "neither frivolous nor out of bounds." *Chamber of Commerce*, 412 F.3d at 144-45; *Yakima Valley Cablevision, Inc.* v. *FCC*, 794 F.2d 737, 746 n.36 (D.C. Cir. 1986) (noting that "[t]he failure of an agency to consider obvious alternatives has led uniformly to reversal"). The Commission also failed to consider other "alternatives . . . within the ambit of the existing policy" with respect to Note (e). *Regents*, 140 S. Ct. at 1913. For example, the Commission could have issued supplemental guidance clarifying its meaning and thereby eliminating any supposed "risk of confusion." Ex. 21 at 43,180 (2022 Rule) (citing commenter suggestion of this alternative but declining to address it). All told, "in failing to consider the option to retain" the centerpieces of the 2020 Rule, the Commission "failed to supply the requisite 'reasoned analysis.'" *Regents,* 140 S. Ct. at 1896.

D. The Commission Failed to Treat Similar Stakeholders Similarly (Count VI).

The Commission's rulemaking was arbitrary and capricious for an additional reason: it failed to justify giving similarly situated stakeholders markedly different treatment. "A long line of precedent has established that an agency action is arbitrary when the agency offered insufficient reasons for treating similar situations differently." *Transactive Corp.* v. *United States*, 91 F.3d 232, 237 (D.C. Cir. 1996). The Commission cannot (and does not) justify deferring to PVAB self-regulation when it rejects self-regulation for similar parties, including other participants in the proxy process. Likewise, the Commission cannot (and does not) explain why it discounted the importance of transparency to shareholders here when it has exalted transparency for shareholders in other contexts.

First, the 2022 Rule singles out PVABs for preferential treatment from other regulated parties with respect to self-regulation. The Commission has consistently rejected voluntary regulation in a variety of contexts, including the Regulation Best Interest rule governing brokers, *see* Ex. 40 (84 Fed. Reg. 33,318 (July 12, 2019)), and issuer-climate disclosures, Ex. 41

(Gensler, *Prepared Remarks* (July 28, 2021)) ("When disclosures remain voluntary, it can lead to a wide range of inconsistent disclosures."). Yet here, the Commission asserts that self-imposed standards—which it concedes are far from comprehensive or complete—are sufficient.

Second, the 2022 Rule ignores shareholders' interest in transparency in direct contrast to the Commission's emphasis on transparency in other contexts. Like those going to the voting booth on election day, those entitled to vote at shareholder meetings are not a monolithic group. In light of shareholders' differing missions, the Commission has consistently reiterated the importance of promoting greater transparency so that shareholders can make their own informed decisions on topics subject to their vote. *Id*. (explaining that transparency is at the "heart of the SEC's mission to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation."). The Commission has repeatedly emphasized the importance of informational disclosure to investors during the proxy process specifically. Ex. 51 (*Universal Proxy,* 86 Fed. Reg. 68,330 (Dec. 1, 2021)). For example, the new Universal Proxy Rule requires that all board options be presented to shareholders in a single proxy card. *Id.* at 68,332. Here, in contrast, the Commission decided to *decrease* the information available to shareholders concerning their voting decisions. This unexplained, divergent treatment is yet another "reason for holding" the 2022 Rule "to be an arbitrary and capricious change from agency practice under the [APA]." *Brand X Internet Servs*., 545 U.S. at 981.

CONCLUSION

For the foregoing reasons, the Court should grant summary judgment to Plaintiffs and set aside the 2022 Rule and the order suspending enforcement of the 2020 Rule.[6]

[6] To avoid undue confusion and ameliorate Plaintiffs' members' injuries, Plaintiffs respectfully request that the Court rule expeditiously and well in advance of the 2023 proxy season, which begins in April.

Dated: September 23, 2022

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that, on September 23, 2022, a copy of the foregoing Memorandum in Support of Plaintiffs' Motion for Summary Judgment was filed electronically. Notice of this filing will be sent by operation of the Court's electronic filing system to all parties indicated on the electronic filing receipt. All other parties will be served by regular U.S. Mail. Parties may access this filing through the Court's electronic filing system.

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