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

Re: Enhanced Reporting of Proxy Votes by Registered Management Investment Companies; Reporting of Executive Compensation Votes by Institutional Investment Managers (File No. S7-11-21)

Dear Ms. Countryman:

Better Markets[1] appreciates the opportunity to comment on the above-captioned proposal ("Proposal" or "Release").[2] The Proposal would enhance the disclosures by registered investment companies of how they vote their proxies. It would also implement Section 14A(d) of the Securities Exchange Act of 1934 ("Exchange Act"), which was added by Section 951 of the Dodd-Frank Act. Section 14A(d) requires that institutional investment managers disclose how they vote proxies related to executive compensation matters. Each of these aspects of the Proposal will increase transparency, and accordingly Better Markets supports them. We urge the Securities and Exchange Commission ("SEC") to move expeditiously to finalize both rules and to resist industry pressure to weaken either one.

BACKGROUND

Corporate suffrage is a one of the most fundamental shareholder rights, largely created under state corporate law and a company's own policies but also recognized in the Exchange Act and the federal framework for regulating the U.S. securities markets. In the Committee report that accompanied the Exchange Act, Congress wrote, "fair corporate suffrage is an important right that

1 Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans' jobs, savings, retirements, and more.

2 86 Fed. Reg. 57,478 (Oct. 15, 2021).

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should attach to every equity security bought on a public exchange."[3] Among other things, meaningful exercise of corporate suffrage can help ensure that boards and management are accountable to shareholders and, to an extent, other stakeholders.[4] In addition, shareholders' right to vote not only on the selection of board members but also on the adoption of major corporate policies can help ensure that shareholders have a voice in corporate strategies affecting the company itself, the communities in which they operate, and even in some cases, the world at large.

However, while enhancing the exercise of corporate suffrage by shareholders is an important aspect of ensuring corporate accountability, it is not enough. This is because while, as of 2019, 53% of American households held stock in public companies, only 15% actually held such stock directly, which would allow them to directly participate in corporate elections.[5] Instead, a significant portion of American households hold stock indirectly through a variety of vehicles, such as mutual funds, retirement accounts, index funds, and other types of investment companies (collectively, "funds"). Because funds are the beneficial owners of the securities in question, it is funds that have the right to vote proxies in shareholder elections.[6] However, while it is funds that have the right to vote proxies, it is by and large the individuals invested in those funds—who are trying to save for a home, education, retirement, and other important life goals—whose financial security is impacted by those votes.[7] And it is those individuals who are affected, directly or indirectly, by the corporate policies and strategies that are established largely through the proxy voting process. Accordingly, to ensure that investors have access to critical information about how shares belonging to their fund are voted, in 2003 the SEC promulgated a rule requiring that funds make an annual report on Form N-PX disclosing their proxy voting.[8] As the SEC notes, while these reports have improved transparency into funds' voting practices, they "can be difficult for investors to use and can provide an incomplete picture of funds' voting practices."[9]

A particularly important aspect of the shareholder franchise is input on executive compensation. Misaligned incentives generally and executive compensation policies in particular at many financial institutions motivated corporate leaders to engage in high-risk activities for short-term profit and lucrative bonuses, and those behaviors were a major contributor to the financial crisis. Citigroup CEO Chuck Prince's infamous quote captures much of what went so

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3 *See* H.R. Rep. No. 73-1383, 2d Sess., at 13 (1934).

4 Roberta S. Karmel, *Voting Power Without Responsibility or Risk: How Should Proxy Reform Address the Decoupling of Economic and Voting Rights?*, 55 Vill. L. Rev. 93, 94 (2010) ("The shareholder franchise is regarded as a key accountability mechanism under both state and federal law.").

5 *See* Board of Governors of the Federal Reserve System, *Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances* at 16 ,18, Federal Reserve Bulletin (Sept. 2020), https://www.federalreserve.gov/publications/files/scf20.pdf.

6 Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, 68 Fed. Reg. 6563, 6565 (Feb. 7, 2003).

7 *See id.* at 6564-6565.

8 Release at 57,479.

9 *Id.* at 57,480.

wrong in the suites of the too-big-to-fail banks on Wall Street as they relentlessly sought more profits and more compensation:

> "When the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you've got to get up and dance. We're still dancing."[10]

These short-sighted policies, fueled by misguided competitiveness and greed rather than principles of sound corporate governance, came at the expense of the long-term viability of those institutions, the entire financial system, and, ultimately, the U.S. economy. As a result, the financial crisis of 2008 will ultimately cost over $20 trillion in lost GDP, in addition to the long-lasting suffering experienced by millions of Americans who lost their jobs, savings, and homes. In the Dodd-Frank Act, Congress sought to address these excesses with a variety of provisions aimed at reigning in executive pay. Among these was Section 951, which added Section 14A to the Exchange Act, generally requiring advisory shareholder votes on executive compensation and golden parachutes. Section 14A(d) requires that "institutional investment managers," which includes entities such as investment advisers and pension funds,[11] disclose annually how they have voted on such resolutions.[12] In 2010, the SEC proposed a rule to implement that provision, but that rule has yet to be finalized.[13]

SUMMARY OF PROPOSAL

The SEC proposes to implement Section 14A(d) of the Exchange Act by requiring that institutional investment managers disclose how they voted on say-on-pay resolutions with respect to any security over which the manager has voting power, and exercises that voting power (without regard to whether the manager is required to report the security on its Form 13F, relating to disclosure of securities over which the manager has investment discretion).[14] Further, the Proposal would improve Form N-PX by, among other things:

- Making clear that a reporting fund is entitled to vote on a matter if its relevant portfolio securities are on loan as of the date of the meeting, because the fund could recall those shares and vote them;[15]

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[10] *See* Michiyo Nakamoto and David Wighton, *Citigroup Chief Stays Bullish on Buy-Outs*, Fin. Times (Jul. 9, 2007), https://www.ft.com/content/80e2987a-2e50-11dc-821c-0000779fd2ac.

[11] Specifically, "institutional investment manager" is defined as "any person, other than a natural person, investing in or buying and selling securities for its own account, and any person exercising investment discretion with respect to the account of any other person." 15 U.S.C. § 78m(f)(6)(A).

[12] 15 U.S.C. § 78n-1(d).

[13] Release at 57,480-81.

[14] *Id.* at 57,481-84.

[15] *Id.* at 57,481.

- To the extent any reporting person (*i.e.*, a fund or a manager) did not recall loaned shares to vote them, the Proposal would require disclosure of how many shares were not recalled;[16]
- Requiring reporting persons to use the same language as the issuers' form of proxy to identify proxy voting matters, and further requiring that matters are presented in the same order;[17]
- Requiring reporting persons to categorize each matter from a standard list of categories and subcategories;[18]
- Requiring reporting persons to disclose the number of shares voted (or instructed to be voted, if the fund cannot reasonably determine how many shares were voted), and how those shares were voted (or instructed to be voted, as the case may be);[19] and,
- Requiring that Form N-PX be filed in a "custom eXtensible Markup Language ('XML')-based structured data language,"[20] which facilitates analysis of the data and promotes comparability.

COMMENTS

I. THE COMMISSION MUST REQUIRE INSTITUTIONAL INVESTMENT MANAGERS TO COMPLY WITH SECTION 14A(d) OF THE EXCHANGE ACT WITHOUT EXCEPTION TO ENSURE THAT SAY-ON-PAY VOTES ARE FULLY TRANSPARENT

Section 14A(d) of the Exchange Act, added by the Dodd-Frank Act following the financial crisis, requires that "**[e]very** institutional investment manager subject" to Section 13(f) of the Exchange Act "report at least annually how it voted on **any shareholder vote** pursuant to subsections (a) [relating to approval of compensation] and (b) [relating to shareholder approval of golden parachutes], unless such vote is otherwise required to be reported publicly by rule or regulation of the Commission."[21] This is a straightforward provision, with only one relevant exception—covered managers are not required to specifically comply with Section 14A(d) if they **are already required** to make the same disclosure by some other rule or regulation. In other words, Section 14A(d) clearly evidences Congress's intent that institutional investment managers make complete and fulsome disclosures of their say-on-pay votes.

Nevertheless, in response to the SEC's 2010 proposal, several industry commenters suggested that the SEC's rule should narrow and alter the statutorily required scheme in a number of ways. For example, some commenters suggested that the SEC adopt a *de minimis* threshold,

16 *Id.* at 57,489-90.
17 *Id.* at 57,485-86.
18 *Id.* at 57,586-87.
19 *Id.* at 57,487-89.
20 *Id.* at 57,495-97.
21 15 U.S.C. § 78n-1(d) (emphasis added).

below which a manager would not be required to report its say-on-pay votes.[22] However, as the Commission properly notes in the Release, "a *de minimis* threshold could reduce the value of the say-on-pay disclosure because a fund manager's full voting record would not be available when the threshold applied."[23] Beyond this, moreover, a *de minimis* threshold would be inappropriate because the statute simply does not provide for one. Establishing one would violate both the letter and the spirit of Section 14A(d).

Similarly, some industry commenters suggested that the rule should alter Section 14A(d)'s scope of securities covered so that it would align with the scope of securities the manager is required to report on Form 13F. However, as the SEC notes in the Release, there are at least two problems with this suggestion: (1) Form 13F reports only require disclosure of holdings as of the end of a quarter, meaning securities disposed of before the end of the quarter would not be reflected in data on how they were voted with respect to say-on-pay issues; and (2) Form 13F reports do not reflect when holdings increased or decreased during a quarter but returned to the "baseline" level reported in the prior quarter, which again would potentially exclude some relevant proxy voting data. Because of these shortcomings, the SEC concludes, correctly, that "this approach could exclude a significant number of say-on-pay votes" which "would be inconsistent with the purpose of Section 14A."[24] Ultimately, the SEC must continue to resist industry pressure to alter the scope of Section 14A(d)'s requirement in a way that would subvert the well-considered (and in any event, mandatory) policy choices Congress made when it passed Section 951.

II. THE SEC'S PROPOSED AMENDMENTS TO FORM N-PX WILL IMPROVE ITS USABILITY FOR INVESTORS AND THE PUBLIC

As detailed above, the SEC is also proposing several amendments to Form N-PX. These amendments will enhance the usability of Form N-PX for investors and the public, and accordingly enhance accountability and transparency. Arguably the most important improvements are related to loaned shares, *i.e.*, making clear that funds are "entitled to vote" shares they loaned but did not recall by the record date of the vote, and the related requirement that reporting persons (whether funds or managers) disclose how many shares they loaned but did not recall to vote on relevant matters.[25] As the Release explains, one way funds and managers can make additional money is by engaging in securities lending.[26] However, if the securities remain on loan as of the record date for the relevant vote, the fund or manager will not be able to vote those shares.[27] In order to vote the shares, the fund or manager would need to recall those shares—which could reduce its revenue.[28] Form N-PX does not currently account for loaned securities that are not recalled, a major loophole that the SEC should close as proposed. This will ensure that investors and the public have a more

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22 Release at 57,484.
23 *Id.*
24 *Id.*
25 *Id* at 57,489.
26 *Id.* at 57,480.
27 *Id.*
28 *Id.*

complete picture of how funds' and managers' securities lending activities, in search of revenue, impact their ability to vote shares in their investors' interests.

Another fundamentally important enhancement the SEC proposes to make to Form N-PX is to require that funds or managers disclose the number of shares voted (or instructed to be voted) and how those shares were voted. As the SEC notes, enhancing the quantitative and qualitative elements of Form N-PX will provide investors with more comprehensive information regarding a fund or manager's voting record as well as its decision not to vote its shares.[29] In addition, where the reporting person votes in multiple manners (*i.e.*, voting some shares in favor and some shares against), this enhanced disclosure will allow investors to see the magnitude of the difference.[30] Ultimately, as with the provision on loaned securities, these amendments will provide investors with a more complete and accurate picture of reporting persons' voting behavior. Moreover, the Commission is correct to reject, as it does in the Release, the dubious assertion by industry commenters that these sorts of quantitative and qualitative disclosures would reveal investment strategies, since a variety of other required disclosures, typically required to be made before the Form N-PX disclosure, would reveal much of the information of concern well before the filing deadline for Form N-PX.[31]

Other aspects of the Proposal that will also make Form N-PX more usable for investors should also be adopted. Requiring that reporting persons use the language issuers use to identify proxy voting matters, and to present them in the same order as on the issuers form of proxy, will ensure uniformity across reports concerning the same matters, making it easier to compare how different funds' and managers' voted on the same matters.[32] Finally, requiring that Form N-PX be filed in a structured data language will make it easier for investors to "aggregate and analyze" the reports, further enhancing transparency and accountability.

<u>CONCLUSION</u>

We hope these comments are helpful as the Commission finalizes the Proposal.

Sincerely,

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Senior Counsel

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29 *Id.* at 57,488.
30 *Id.* at 57,487-88.
31 *Id.* at 57,488.
32 *Id.* at 57,486.

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