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# Meridian Client Update

## **SEC Will Not Enforce Rules Governing Proxy Advisory Firms**

**The Securities and Exchange Commission's (SEC) Division of Corporation Finance will not enforce new rules regulating proxy advisory firms ("PAFs") during the time in which the SEC revisits and evaluates these rules.**

Whether PAFs should be subject to a rigorous regulatory regime has been a political football for some time, with Republicans generally calling for enhanced regulations and Democrats preferring light touch regulations. This partisan split was on full display on June 1, 2021 when SEC Chair Gary Gensler directed the Division of Corporation Finance to consider whether to recommend that the SEC revisit regulations of PAFs adopted by the Republican-controlled SEC just last year.

In 2020, the SEC adopted amendments to several of its Rules ("2020 Amendments")<sup>1</sup> that subjects PAFs to a new regulatory regime. At a high level, the 2020 Amendments:

- Codify the SEC's 2019 interpretive guidance ("2019 Guidance") that proxy voting advice generally constitutes a solicitation within the meaning of the Securities Exchange Act of 1934<sup>2</sup>, which makes such advice subject to the anti-fraud provisions of Rule 14a-9 (effective November 2, 2020).
- Amend the proxy rules to clarify when the failure to disclose certain information in proxy voting advice may be considered misleading within the meaning of the rules (e.g., a PAF's proxy voting advice that fails to include certain information, such as methodology used to determine vote recommendations) (effective November 2, 2020).
- Condition the availability of certain existing exemptions from the information and filing requirements of the federal proxy rules for PAFs upon compliance with additional disclosure and procedural requirements, effective December 31, 2021 ("Exemption Conditions") (see our [Client Update dated August 4, 2020](#) and the attachment to this Client Update for additional details on the Exemption Conditions). Among other things, the Exemption Conditions will require a PAF:
  - To disclose conflicts procedures and existing conflicts of interests, as determined by the PAF,
  - To adopt written policies and procedures designed to ensure that the PAF's proxy voting advice is made available to registrants at or prior to the time when such advice is disseminated to the PAF's clients, and

<sup>1</sup> Specifically, on July 23, 2020, the SEC adopted amendments to Rules 14a-1(l), 14a-2(b), and 14a-9.

<sup>2</sup> On August 21, 2019, the SEC issued interpretive guidance clarifying that a PAFs' proxy voting advice generally constitutes a solicitation within the meaning of the Securities Exchange Act of 1934. The SEC's amendment to Rule 14(a)-1(l)(iii) codifies this Guidance.

- To adopt written policies and procedures designed to ensure that the PAF provides clients with a registrant’s views about the PAF’s proxy voting advice, so that they can take such views into account as they vote their proxies.

These rules are now on hold and will not be enforced during the period in which the SEC is considering further regulatory action in this area. In addition, in the event that new regulatory action leaves the Exemption Conditions in place with the current December 1, 2021 compliance date, the SEC staff will not recommend any enforcement action based on those Exemption Conditions for a reasonable period of time after any resumption by Institutional Shareholder Services Inc. of its litigation challenging the 2020 Amendments and the 2019 Guidance.

**Meridian comment.** The SEC’s adoption of the 2020 Amendments represented the culmination of a years’ long effort by issuers, as well as corporate organizations such as the U.S. Chamber of Commerce, to require greater transparency and accountability of PAFs. However, Democratic Commissioner Allison Herren Lee criticized the 2020 Amendments as “unwarranted, unwanted, and unworkable.” In addition, many institutional shareholders, Congressional Democrats and other stakeholders have not favored additional regulations of PAFs, particularly any regulations that may potentially add costs for investors and/or compromise the independence of PAFs. This antipathy toward the 2020 Amendments could conceivably result in the SEC withdrawing (rather than modifying) the 2020 Amendments. The SEC has earmarked April 2022 as the target date for any potential proposed revisions to the 2020 Amendments.

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The **Client Update** is prepared by Meridian Compensation Partners’ Governance and Regulatory Team led by Donald Kalfen. Questions regarding this Client Update or executive compensation technical issues may be directed to Donald Kalfen at 847-235-3605 or dkalfen@meridiancp.com.

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## Attachment

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### PAFs' Exemption from Proxy Rules Conditioned on Compliance with Certain Disclosure and Procedural Requirements

Historically, the SEC has exempted certain kinds of solicitations from the proxy rules (e.g., information and filing requirements). For example, the SEC has exempted communications by persons not seeking proxy authority and proxy voting advice given by advisors to their clients under certain circumstances. PAFs have historically relied on these exemptions to provide proxy voting advice, without the necessity of complying with the filing and information requirements of the proxy rules.

The 2020 Amendments make these exemptions conditioned upon a PAF's compliance with the following requirements, which are further described below: (i) disclosure of conflicts procedures, (ii) adoption of written policies and procedures designed to ensure that the PAF's proxy voting advice is made available to registrants and (iii) adoption of written policies and procedures designed to ensure that the PAF provides clients with a registrant's views about the proxy voting advice, so that they can take such views into account as they vote proxies.

### Disclosure of Conflicts Procedure and Actual Conflicts of Interest ("Conflicts Rule")

A PAF must include in its proxy voting advice (or in any electronic medium used to deliver the advice) prominent disclosure of:

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

The Conflicts Rule allows a PAF to apply its judgment and unique knowledge of the facts to determine whether a disclosable conflict exists.

### Delivery of Proxy Voting Advice to Registrants

A PAF is required to adopt and publicly disclose written policies and procedures that ensure proxy voting advice is made available to each applicable registrant **at or prior to the time when such advice is disseminated** to the PAF's clients.

However, PAFs are under no obligation to:

- Allow registrants the opportunity to review proxy voting advice in advance of its distribution to the PAF's clients (although the SEC encourages PAFs to do so to the extent feasible), or
- Provide registrants additional versions of its proxy voting advice with respect to the same meeting, vote, consent or authorization, as applicable, if the advice is subsequently revised (however, PAFs, in their sole discretion, may provide such additional versions to registrants).

Under a safe harbor, a PAF will be deemed to satisfy the above requirements if it maintains written policies and procedures that provide a registrant with a copy of the PAF's proxy voting advice, at no charge, no later than the time such advice is disseminated to the PAF's clients. Such policies and procedures may include conditions requiring that:

- The registrant has filed its definitive proxy statement at least 40 calendar days (or such shorter time period, as specified in the PAF's discretion) before the meeting, or if no meeting is held, at least 40 calendar days before the date the votes, consents, or authorizations may be used to effect the proposed action; and
- The registrant has acknowledged that it will only use the copy of the proxy voting advice for its internal purposes and/or in connection with the solicitation and such copy will not be published or otherwise shared except with the registrant's employees or advisers.

### **Registrant Feedback and Delivery to PAFs' Clients**

A PAF is required to implement procedures to:

- obtain registrant feedback on the PAF's proxy voting advice; and
- disseminate that feedback to its clients, in a timely manner before the shareholder meeting.

Under a safe harbor, a PAF will be deemed to satisfy the above requirements by (i) maintaining written policies and procedures that (A) reflect the above requirements, and (B) informing clients who receive proxy voting advice when a covered registrant notifies the PAF that it intends to file or has filed additional soliciting materials with the registrant's statement regarding the proxy voting advice and (ii) providing notice to its clients on its electronic platform or through email or other electronic means.

However, the 2020 Amendments do not:

- Prescribe the manner or specific timing in which a PAF must obtain a registrant's feedback, or
- Require a PAF to consider or otherwise take into account in registrants' feedback.