Council of Institutional Investors®
The voice of corporate governance

CII Fact Sheet on Proxy Advisory Firms and Shareholder Proposals
Nov. 5, 2019

1. **The Business Roundtable, National Association of Manufacturers and other management groups' claim that proxy advice is rife with errors is based on anecdote not evidence.**

   - The SEC comment file for the SEC's Nov. 15, 2018, proxy roundtable includes a number of letters that assert that errors in proxy reports are endemic. But the letters offer very few examples and most of those do not identify the company and cannot be checked. CII believes most claims of errors actually are methodological differences.

   - The only study that CII is aware of that purports to tote up proxy advisor errors alleges just 39 factual errors over nearly three years (or 0.1% of more than 30,000 reports by leading proxy advisory firms Institutional Shareholder Services (ISS) and Glass Lewis during that period). And the study inflates the claimed error rate. CII's own analysis of the study found that no more than 17 of the claims of factual error had merit.

   - CEO and board member dislike of proxy advisors appears driven by discomfort with the role of proxy research to be critical and raise questions. The charge of systemic factual error appears to be fabricated as a means to quash critical analysis and commentary.

2. **Claims that proxy advisory firms wield excessive influence over how institutional investors vote confuse correlation with causation.**

   - Many pension funds and other institutional investors buy proxy and review advisors' research and recommendations but vote according to their own guidelines and policies. According to ISS, 85% of its top 100 clients use a custom voting policy.

   - It is wrong and insulting to suggest that institutional investors "robo vote"—vote in lockstep with proxy advisor recommendations. While ISS recommended voting against say-on-pay proposals at 12.3% of Russell 3000 companies in 2018, just 2.4% of those companies received less than majority shareholder support on their say-on-pay proposals. In 2019, Glass Lewis recommended in favor of 89% of directors and 84% of say-on-pay proposals, while directors received average support of 96% and say-on-pay proposals garnered average support of 93%.

   - Academic research has found that while both ISS and Glass Lewis appear to have some impact on shareholder voting, media reports often substantially overstate the extent of that influence.

3. **The proposed mandate that proxy advisory firms let companies review the firms' reports before investor clients see them amounts to unprecedented interference in the free market and is the opposite of what is required by regulation of stock analyst reports.**

   - Current rules prohibit analysts from sharing draft research reports with target companies, other than to check facts after approval from the firm's legal or compliance department.

   - FINRA Rule 2241, which the SEC approved, establishes this safeguard to, as the SEC has explained, "help protect research analysts from influences that could impair their objectivity and independence."

   - If the SEC adopts its proxy advisor regulation, an analyst and a proxy advisor could write a report on the same company and the analyst would violate securities laws by showing it to the company in advance, while the proxy adviser would violate the law if it *did not* show it to the company in advance.

   - This is the very definition of arbitrary and capricious government action.

4. **Three SEC commissioners are attempting to jam through fundamental changes without appropriate analysis and public comment.**

   - The predicate for the SEC's new, heavy-handed regulatory structure for proxy advisory firms is a significant change made by the SEC on Aug. 15, 2019, on a 3-2 vote, without any public comment, zero cost-benefit analysis and limited and flawed legal justification.

5. **Shareholder proposals have proven to be a key channel for effective shareholder engagement with public companies for more than half a century.**

   - Shareholder proposals permit investors to express their voice collectively on issues of concern to them, without the cost and disruption of waging proxy fights.

   - Shareholder proposals have encouraged many companies to adopt governance policies that today are viewed widely as best practice.
     - Electing directors by majority vote, rather than by plurality, a radical idea a decade ago when shareholders pressed for it in proposals, is now the norm at 90% of large-cap U.S. companies.
     - Similarly, norms such as independent directors constituting a majority of the board, independent board leadership, board diversity, sustainability reporting, non-discrimination policies and annual elections for all directors all were advocated early through shareholder proposals.

   - Shareholder proposals are a critical tool for expression of the collective views of holders, permitting them to communicate with each other as well as the company on whether an issue or approach has support. Another tool is voting against directors, but the message from negative voting on directors when the concern is a specific policy or disclosure is much less focused or clear.

6. **Shareholder proposals are not a significant burden to U.S. public companies.**

- Shareholder proposals are almost always non-binding. The board actually does not have to do anything in response to a proposal.

- Most public companies do not receive any shareholder proposals. On average, 13% of Russell 3000 companies received a shareholder proposal in a particular year between 2004 and 2017. In other words, the average Russell 3000 company can expect to receive a proposal once every 7.7 years. For companies that receive a proposal, the median number of proposals is one per year.

- Companies exaggerate the cost of shareholder proposals. Most of the cost involves attempts by management to exclude proposals from their proxy statements, which is a choice made by management. The cost to put a proposal on the proxy ballot is *de minimis*.

- CEO advocacy organizations say that shareholder proposals keep private companies from doing an IPO, an unsupportable and fact-free assertion. It is ludicrous to argue that a board would forgo access to public capital markets because in the next eight years the company may face a nonbinding shareholder proposal requesting better disclosure on its carbon footprint or the annual election of all directors.

7. **Additional curbs on shareholder proposals are not needed.**

- Raising resubmission thresholds will stifle new ideas and issues, which typically take time to gain traction with investors.

- The raised resubmission thresholds will keep topics off corporate ballots for years, even though circumstances may change at a company (e.g., independent board leadership tends to be seen as much more urgent when a company is in crisis, and the proposed new thresholds are likely to bar a proposal to separate the roles of CEO and chair at companies with the worst governance records).

- The increased ownership thresholds will especially hamper small investors, the very market participants that SEC Chairman Jay Clayton has made it a priority to protect.

- Until 1983, ownership of a single share of stock carried the right to propose a shareholder resolution. Now we are on a slippery slope that strips that right from more and more small shareholders, whose ideas can be as important and valuable to consider as those of larger holders.