

Via E-Mail

April 27, 2021

The Honorable Sherrod Brown
Chairman
Committee on Banking, Housing & Urban Affairs
United States Senate
Washington, DC 20510

The Honorable Patrick J. Toomey
Ranking Member
Committee on Banking, Housing & Urban Affairs
United States Senate
Washington, DC 20510

Re: Support for S.J. Res. 16

Dear Mr. Chairman and Ranking Member Toomey:

I am writing on behalf of the Council of Institutional Investors (CII) to express our strong support for S.J. Res. 16,¹ the Congressional Review Act (CRA) disapproval of the Securities and Exchange Commission's (SEC or Commission) shareholder proposal rule amendments (2020 Amendments).²

CII is a nonprofit, nonpartisan association of United States (U.S.) public, corporate and union employee benefit funds, other employee benefit plans, state and local entities charged with investing public assets, and foundations and endowments with combined assets under management of approximately \$4 trillion. Our member funds include major long-term shareowners with a duty to protect the retirement savings of millions of workers and their families, including public pension funds with more than 15 million participants – true “Main Street” investors through their pension funds. Our associate members include non-U.S. asset owners with about \$4 trillion in assets, and a range of asset managers with more than \$40 trillion in assets under management.³

¹ S.J. Res. 16, 117th Cong. (intro. Mar. 25, 2021), <https://www.congress.gov/bill/117th-congress/senate-joint-resolution/16/text> (“Providing for congressional disapproval under chapter 8 of title 5, United States Code, of the rule submitted by the Securities and Exchange Commission relating to ‘Procedural Requirements and Resubmission Thresholds Under Exchange Act Rule 14a-8’”).

² Procedural Requirements and Resubmission Thresholds Under Exchange Act Rule 14a-8, Exchange Act Release No. 89,964, 85 Fed. Reg. 70,240 (Sept. 23, 2020), <https://www.govinfo.gov/content/pkg/FR-2020-11-04/pdf/2020-21580.pdf>.

³ For more information about the Council of Institutional Investors (“CII”), including its board and members, please visit CII’s website at <http://www.cii.org>.

CII believes the existing shareholder proposal process has long been a cost-effective way for shareholders to communicate with each other and for shareholders as a group to communicate with management on important issues that can protect and drive long-term shareholder value and benefit the U.S. capital markets.⁴

The 2020 Amendments were opposed by CII and most investors and other market participants,⁵ in part, because they would result in a process that is more complicated, more constricting and more costly.⁶ In addition, the 2020 Amendments were adopted through a rulemaking process that the SEC's own Office of Investor Advocate (SEC Investor Advocate) found to be "fundamentally flawed."⁷ For these and other reasons, CII has concluded that the 2020 Amendments are an appropriate candidate for CRA disapproval.⁸

Benefits of the shareholder proposal process

CII members believe that effective corporate governance and disclosure serve the best long-term interests of companies, shareowners and other stakeholders.⁹ Effective corporate governance helps companies achieve strategic goals and manage risks by ensuring that shareowners can hold directors to account as their representatives, and in turn, directors can hold management to account, with each of these constituents contributing to balancing the interests of the company's varied stakeholders.¹⁰

CII members use a variety of stewardship tools to improve corporate governance and disclosure at the companies they own.¹¹ These tools include casting well-informed proxy votes; engaging in dialogue with portfolio companies (including with board members, as appropriate), external managers and policymakers; filing shareowner resolutions; nominating board candidates;

⁴ See Press Release, Council of Institutional Investors, SEC Muzzles the Voice of Investors by Raising the Bar on Shareholder Proposals (Sept. 23, 2020), https://www.cii.org/sept23_sec_muzzles ("For decades, the shareholder proposal process has been a well-functioning pillar of corporate governance in U.S. capital markets [and] [i]t is a cost-effective way for shareholder[s] to communicate with each other and for shareholders as a group to communicate with management through votes on proposals.")

⁵ See Commissioner Allison Herren Lee, Statement on the Amendments to Rule 14a-8 (Sept. 23, 2020), <https://www.sec.gov/news/public-statement/lee-14a8-2020-09-23> ("Individual investors, asset managers, pension funds and labor unions representing the interests of teachers, firefighters, and service employees, state and local governments, universities, religious institutions, numerous investor organizations representing trillions of dollars in assets under management, US Senators, academics, a Commissioner at the Federal Election Commission, state securities regulators, our own Investor Advisory Committee—shareholders of every ilk and many others wrote in overwhelming numbers to urge us not to adopt these amendments.")

⁶ See Press Release, Council of Institutional Investors, SEC Muzzles the Voice of Investors by Raising the Bar on Shareholder Proposals ("The amendments weaken the voice of investors and jeopardize faith in the fairness of U.S. public capital markets by making the filing process more complicated, constricting and costly . . .").

⁷ U.S. Securities and Exchange Commission, Office of Investor Advocate, Report on Activities, Fiscal Year 2020 at 5 (Dec. 29, 2020), <https://www.sec.gov/advocate/reportspubs/annual-reports/sec-investor-advocate-report-on-activities-2020.pdf>.

⁸ Cf. Kobi Kastiel & Yaron Nili, The Giant Shadow of Corporate Gadflies, Harv. L. Sch. F. on Corp. Governance (Apr. 21, 2021), <https://corpgov.law.harvard.edu/2021/04/21/the-giant-shadow-of-corporate-gadflies/> (concluding that: "[News of potential repeal](#) of the SEC rules are a positive development").

⁹ See Council of Institutional Investors, Corporate Governance Policies 4 (updated Sept. 22, 2020), https://www.cii.org/files/policies/09_22_20_corp_gov_policies.pdf ("CII believes effective corporate governance and disclosure serve the best long-term interests of companies, shareowners and other stakeholders").

¹⁰ *Id.*

¹¹ *Id.*

litigating meritorious claims; and retaining or dismissing third parties charged with assisting in carrying out these activities.¹²

The value of shareholder proposals as a means of communication is not limited to shareholders engaging with management and boards. Proposals allow shareholders to speak to, inform and test the waters on an issue with their fellow shareholders. A company's proxy materials tell shareholders what the company wants them to know; a shareholder proposal alerts all shareholders to an issue that their fellow shareholders think is important—and invites their input on the topic. It may be in the self-perceived interest of some managers or board members to totally control the flow of information to a company's shareholders, but such a result is not in the interest of shareholders as a whole. Keeping the lines of communication open is important in a marketplace that has substantial restrictions on communications between shareholders.

Over the past three decades in particular, the communications resulting from shareholder proposals have been the most important vehicle by which shareholders raised—and helped change—corporate policies on a wide range of core governance issues, including majority voting for and annual election of directors, independent board leadership, appropriate forms of compensation of outside directors, proxy access, board diversity, clawbacks of unearned executive compensation, appropriate accounting for stock options, fair employment practices and meaningful sustainability reporting. And, importantly, these improvements to corporate governance were generally achieved without the cost and disruption of waging proxy fights.

Lack of evidence of a problem with the existing rule

CII believes SEC Rule 14a-8 was working well prior to the 2020 Amendments. Some corporate lobbyists for management interests have vastly exaggerated the extent to which shareholder proposals are used. As institutional investors who vote proxies know, shareholder proposals make up less than 2% of voting items, and the vast majority of their time is spent reviewing *management* proposals.¹³

Some commentators also seem to miss that nearly all shareholder proposals are non-binding—they are simply requests from shareholders for the board to consider some policy, practice or idea. The effort by some corporate lobbyists to restrict Rule 14a-8 by supporting the 2020 Amendments likely relates to the fact that shareholder proposals get much more support now than in decades past.¹⁴ We believe that rising support levels indicate the shareholder proposal rule was working.

¹² *Id.*

¹³ *See, e.g.,* Ning Chiu, Davis Polk, How Funds View and Vote on Shareholder Proposals, Briefing: Governance (Nov. 12, 2018), <https://www.briefinggovernance.com/2018/11/how-funds-view-and-vote-on-shareholder-proposals/> (“Shareholder proposals make up less than 2% of the total number of ballot items.”).

¹⁴ *See, e.g.,* Yaron Nili & Kobi Kastiel, The Giant Shadow of Corporate Gadflies, 94 S. Cal. L. Rev. 13 (forthcoming 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3520214 (“Although the number and proportion of governance-related proposals has decreased slightly recently, the support these proposals receive continues to remain high, growing from 5% in 1994 to 38% in 2019.”).

As SEC Commissioner Allison Herren Lee pointed out:

It is exceedingly rare for most companies to receive a shareholder proposal at all. An analysis of Russell 3000 companies reveals that, on average, only 13 percent of companies received a shareholder proposal in a particular year between 2004 and 2017. That translates to approximately one proposal every 7.7 years for the average company.¹⁵

In CII's view this is no evidence of a "problem" that needs to be solved and certainly not on a market-wide basis. In addition, the "problem" is hardly getting worse—quite the opposite, in fact.¹⁶ A 2020 report by Sullivan & Cromwell LLP (S&C Report) concluded:

Overall, the total number of shareholder proposals declined, continuing a downward trend that began in 2015. A total of 657 shareholder proposals have been submitted to date in 2020, relative to 678 at this time last year, 722 for 2019 as a whole and 788 for 2018.¹⁷

Moreover, the level of support for shareholder proposals in most cases remains strong. The S&C Report breaks down the 2020 level of support as follows:

Environmental, social and political (ESP) proposals:

- Total ESP submissions decline, but percentage voted and number of passing proposals increase
- Environmental proposals predominate ESP submissions, as demand for climate change and other ESP reporting increases and proposals for adoption of Sustainability Accounting Standards Board and Task Force on Climate-Related Financial Disclosures standards typically receive over 60% support
- Political and lobbying proposals decrease in number but are voted at a record rate (over 80%), with five passing (most since 2014)

....

Governance proposals:

....

- Independent chair proposals decrease (by 30%) but receive higher average support[.]¹⁸

If the "problem" perceived by the 2020 Amendments—too many proposals from too many small shareholders—is, at most, isolated to only a handful of very large companies with resources to respond, why should the Commission change the rule to affect the thousands of publicly traded

¹⁵ Commissioner Allison Herren Lee, Statement on the Amendments to Rule 14a-8 (footnotes omitted).

¹⁶ *See id.* ("the Commission's own analysis shows that the number of overall shareholder proposals has been trending down in recent years and, as of the 2018 proxy season, was at roughly the same level as in 1997").

¹⁷ Sullivan & Cromwell LLP, 2020 Proxy Season Review: Part I, Rule 14a-8 Shareholder Proposals 1 (July 15, 2020), <https://www.sullcrom.com/files/upload/SC-Publication-2020-Proxy-Season-Review-Part-1-Rule-14a-8.pdf>.

¹⁸ *Id.* at cover page.

companies that rarely, if ever, receive a shareholder proposal? The 2020 Amendments have no answer.

Some lobbyists for corporate executives have suggested there is a particular problem with shareholder proposals that raise issues related to environmental and social impacts on company performance, and that this problem justifies limiting shareholder proposal rights in general (including corporate governance proposals). For example, the Business Roundtable—which advocates mainly for large company CEOs and arguably was the key lobbying group spurring the current efforts to reduce shareholder proposal rights—says the shareholder proposal process needs “modernization” because the thresholds for resubmission of proposals are too low and because “excluding proposals relating to general social issues is difficult for companies.”¹⁹

It is true that all social policy proposals could be excluded before 1970, based on SEC precedents that permitted Greyhound Corp. in the late 1940s and early 1950s to exclude shareholder proposals urging the company to desegregate buses.²⁰ Those proposals may have been viewed at the time as “idiosyncratic,” with “no rational relationship to the creation of long-term shareholder value” and in “conflict with what a typical investor views as material to making an investment or voting decision,” to use the Business Roundtable’s words on recent social policy matters implicated in shareholder proposals.²¹ However, in our view, “those proposals were prescient, dealt with a socially important issue with long-term implications both for society and for shareholder value, and were material to how Greyhound Corp. operated.”²²

Current data suggests that companies are increasingly engaging in dialogue with proponents and are recognizing the value of folding ESP considerations into their daily operations.²³ Some have referred to a shift in corporate attitudes as a “new paradigm.”²⁴ This would not appear to be the

¹⁹ Letter from Business Roundtable to Mr. Brent J. Fields, Secretary, Securities and Exchange Commission 4 (Nov. 9, 2018), https://s3.amazonaws.com/brt.org/2018.11.09-BRT_SECProxyRoundtableCommentLetter.pdf.

²⁰ See Kenneth Propp, *The SEC as Referee: Managing the Shareholder Resolution Process* 4 (Sept. 1980) (on file with CII) (“The lack of [SEC] guidance offered by the [14a-8] ‘proper subject’ test became apparent in 1947 when the SEC was faced with a request by Greyhound Corp. to exclude a resolution asking it to abolish segregated seating on its buses The SEC excluded the resolution, saying it had been submitted for racial reasons. Five years later, in 1952, 14a-8 was amended to exclude resolutions in which ‘it clearly appears that the proposal is submitted by the security holder. . . primarily for the purpose of promoting general economic, political, racial, religious, social or similar causes.’”).

²¹ Letter from Business Roundtable to Mr. Brent J. Fields, Secretary, Securities and Exchange Commission at 4.

²² Letter from Kenneth A. Bertsch, Executive Director, Council of Institutions Investors et al. to Vanessa A. Countryman, Secretary, Securities and Exchange Commission 9 (Jan. 30, 2020), <https://www.sec.gov/comments/s7-23-19/s72319-6729684-207400.pdf>.

²³ See Commissioner Allison Herren Lee, Statement on the Amendments to Rule 14a-8 (“Climate change, workforce diversity, independent board leadership, and corporate political spending, as well as other ESG-related issues, are increasingly important to investors—and increasingly present on proxy ballots.”).

²⁴ Marty Lipton, Wachtell, Lipton, Rosen & Katz, *It’s Time to Adopt the New Paradigm*, Harv. L. Sch. F. on Corp. Governance (Feb. 11, 2010) <https://corpgov.law.harvard.edu/2019/02/11/its-time-to-adopt-the-new-paradigm/> (commenting that companies and investors alike have been rethinking the ways in which they engage and have been providing robust and increasingly tailored disclosures about their approaches to strategy, purpose, and mission; board involvement, composition and practices; board oversight of strategy and risk management; the business case for long-term investments, reinvesting in the business and retraining employees, pursuing R&D and innovation, and other capital allocation priorities; sustainability, ESG and human capital matters; stakeholder and shareholder relations; corporate governance; corporate culture; and other matters that are integral to the new paradigm).

time to turn off the spigot, as the 2020 Amendments would inevitably do—and is intended to do—for a number of shareholder proposals.

Impact of the 2020 Amendments

As indicated, the 2020 Amendments make it easier for public companies to exclude shareholder proposals from corporate proxy statements. The Commission accomplished this by among other changes: (1) raising the ownership thresholds that an investor must meet to submit a proposal for a vote by fellow shareholders;²⁵ and (2) raising the levels of shareholder support a proposal must receive to be eligible for resubmission at the same company's future shareholders' meetings.²⁶

CII generally agrees with the observation of the SEC's Investor Advocate in his annual report to the U.S. Congress that:

[T]he new ownership thresholds significantly diminish the ability of shareholders with smaller investments to submit proposals. The comment file is replete with evidence demonstrating that shareholders with smaller investments have played an important role in the shareholder-proposal process, including by submitting proposals that have garnered broad shareholder support.²⁷

Consistent with the SEC Investor Advocate's observation, empirical evidence indicates that “by making the barriers to submission higher and more costly [for small investors, the 2020 Amendments] . . . may lead to significant reduction in the adoption of governance practices that large investors overwhelming support.”²⁸

In addition, CII research found that the 2020 Amendments' new thresholds for resubmitting shareowner resolutions would have more than doubled the number of excluded governance proposals in 2011-2019.²⁹ In particular, the new thresholds would have reduced the number of proposals for independent chairs and to improve disclosure on political contributions and lobbying.³⁰ This is a conservative estimate based on retroactive application of the changes.

²⁵ 85 Fed. Reg. at 70,244 (“Under new Rule 14a-8(b), a shareholder will be eligible to submit a Rule 14a-8 proposal if the shareholder demonstrates continuous ownership of at least: • \$2,000 of the company's securities entitled to vote on the proposal for at least three years; • \$15,000 of the company's securities entitled to vote on the proposal for at least two years; or • \$25,000 of the company's securities entitled to vote on the proposal for at least one year.”).

²⁶ *Id.* at 70,256 (“We proposed to amend the resubmission thresholds under Rule 14a-8(i)(12); specifically, we proposed to replace the thresholds of 3, 6, and 10 percent with thresholds of 5, 15, and 25 percent, respectively.”).

²⁷ U.S. Securities and Exchange Commission, Office of the Investor Advocate, Report on Activities, Fiscal Year 2020 at 3.

²⁸ Kobi Kastiel & Yaron Nili, The Giant Shadow of Corporate Gadflies, Harv. L. Sch. F. on Corp. Governance.

²⁹ See Ernie Barkett, Council of Institutional Investors, The SEC's Proposed Rule to Curb Shareholder Proposals 5 (Apr. 2020), https://www.cii.org/files/publications/misc/CII_14a-8_Issue_Brief%20April_2020_FINAL.pdf (“we find that the new thresholds would have more than doubled the number of excluded proposals in the period, from 221 to at least 514.”).

³⁰ See *id.* at 6.

Our research also identified investor concern relating to the 2020 Amendments' failure to address the impact of the new thresholds on dual-class stock companies.³¹ We believe the "current thresholds already are high for many or most dual-class stock companies."³²

Companies have substantial opportunity to influence votes at the margins of a threshold. Therefore, it is likely that companies will take extra steps to depress votes that are marginally more than 15% in the second year that they come to a vote, or 25% in the subsequent year.

Moreover, many important 2020 governance proposals that would have been eligible for resubmission in 2021 would be blocked by the new resubmission thresholds starting in 2022:

- Require independent board chairs (Facebook, Southwest Airlines, Tenet Healthcare)
- Report on incentive-based compensation and risks of material losses (Wells Fargo)
- Consider employee pay in setting CEO pay (3M, Mondelez International)
- Institute a majority vote standard for election of directors (Sinclair Broadcast Group)
- Provide shareholders the right to act by written consent (Cognizant Technology Solutions Group, Kohl's, Norfolk Southern, Pfizer)
- Reduce threshold for shareholders to call special meeting (Howmet Aerospace, Lincoln National)
- Take steps to consolidate share classes to have one vote per share (Coca-Cola Consolidated, Tyson Food).

Proposals related to ESP matters will also be sharply curtailed at a time when significant threats to shareholder value stemming from such issues have emerged, including risks related to the Covid-19 pandemic, lack of diversity and inclusion, poor human capital management practices and climate change. We generally agree with SEC Commissioner Lee that the "Commission should be encouraging this kind of engagement, not stifling it."³³

The SEC's rulemaking process was flawed

When the 2020 Amendments were approved CII expressed the view that the "SEC breached its own stated procedures for using economic analysis in rulemaking and failed to grapple with the damaging impacts investors cited or to justify the changes."³⁴ As indicated, last December, our view was confirmed by the SEC's Investor Advocate.³⁵

³¹ See *id.* at 7.

³² *Id.*; see generally, Jeffrey P. Mahoney, General Counsel. Council of Institutional Investors to The Honorable Sherrod Brown, Chairman, Committee on Banking, Housing & Urban Affairs, United States Senate et al. 2-5 (Mar. 18, 2021), https://www.cii.org/files/issues_and_advocacy/correspondence/2021/2021%20Investor%20Advocate%20Letter.pdf (discussing the need for, and proposing, reforms of dual-class stock companies).

³³ See Commissioner Allison Herren Lee, Statement on the Amendments to Rule 14a-8.

³⁴ Press Release, Council of Institutional Investors, SEC Muzzles the Voice of Investors by Raising the Bar on Shareholder Proposals.

³⁵ U.S. Securities and Exchange Commission, Office of the Investor Advocate, Report on Activities, Fiscal Year 2020 at 3-4.

In his annual report to the U.S. Congress, the SEC's Investor Advocate recommended that the 2020 Amendments should be overturned or reversed explaining:

. . . [W]e believe the economic analysis in this rulemaking was fundamentally flawed. For example, the Commission sought to raise the ownership thresholds to account for inflation since the thresholds were last adjusted in 1998, even though the number of shareholder proposals had trended downward over the years despite the effects of inflation. The Commission also ascribed little value to shareholder proposals that failed to receive a majority vote at a shareholder meeting, even though commenters provided numerous examples of shareholder proposals that led to constructive governance reforms before receiving a formal majority vote.

. . . .

. . . Our Office is charged with analyzing the potential impact on investors of rulemaking proposals and making recommendations to the Commission regarding those proposals. Exchange Act Section 4(g)(5) directs the Commission to ensure that the Investor Advocate has "full access" to the documents of the Commission as necessary to carry out the functions of the Office. Pursuant to this authority, we repeatedly requested copies of DERA's written analysis to no avail, until the Commission quietly submitted the analysis into the public comment file more than nine months later.

*In sum, we believe this particular rulemaking was adopted in contravention of the Commission's internal policies for full and objective economic analysis, Exchange Act Section 4(g)(5), and, at the very least, the spirit of the Administrative Procedure Act. In our view, investors should not have to bear the expense of litigation to overturn such a flawed rulemaking.*³⁶

For all of the above reasons, CII urges the members of your Committee to vote "Yes" on S.J. Res. 16. If we can answer any questions or provide any additional information about CII's strong support for S.J. Res. 16, please do not hesitate to contact me.

Sincerely,



Jeffrey P. Mahoney
General Counsel

³⁶ *Id.* (emphasis added).