Exhibit 1

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

INSTITUTIONAL SHAREHOLDER SERVICES INC., *Plaintiff*, v. SECURITIES AND EXCHANGE COMMISSION and WALTER JOSEPH CLAYTON III in his official capacity as Chairman of the Securities and Exchange Commission, *Defendants*.	§ § § § § § § § § § § § § §	Case No. 1:19-cv-3275-APM

BRIEF AMICI CURIAE OF THE COUNCIL OF INSTITUTIONAL INVESTORS ET AL. IN SUPPORT OF PLAINTIFF

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INTEREST OF AMICI CURIAE

The Council of Institutional Investors (CII or Council) is a nonprofit, nonpartisan association of 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. Its associate members include non-U.S. asset owners with more than $4 trillion in assets and a range of asset managers with more than $40 trillion in assets under management. The Council's hundreds of members share a commitment to healthy public capital markets and strong corporate governance. Those members include major long-term shareowners with duties to protect the retirement assets of millions of American workers and their families, including public pension funds with more than 15 million participants—true "Main Street" investors who rely on their hard-earned pension funds. The Council's members work to protect those assets through proxy votes, stockholder resolutions, negotiations with regulators, discussions with management and boards, and, when necessary, litigation. The Council is thus a leading voice for effective corporate governance, strong stockholder rights, and vibrant, transparent, and fair capital markets, and it regularly advocates on behalf of these goals to Congress, the Securities and Exchange Commission (SEC), and state and federal courts.

The additional amici are the California Public Employees' Retirement System (CalPERS), the California State Controller, the California State Teachers' Retirement System (CalSTRS), the CFA Institute, the Colorado Public Employees'

Retirement Association (PERA), the Comptroller of the City of New York, the CtW Investment Group, and the Los Angeles County Employees Retirement Association (LACERA). Each of these amici is a member of the Council and is described more specifically in the appendix.

The issue before the Court directly implicates the interests of the Council and amici.[1] Institutional investors bear, and faithfully execute, fiduciary duties to the millions of individuals on whose behalf they manage funds. Among those fiduciary duties is the obligation to vote fund securities in the best interests of the fund's beneficiaries. However, because institutional investors commonly hold hundreds or thousands of different portfolio securities, it would be prohibitively expensive and economically inefficient for every institutional investor to perform individually the research and analysis necessary to cast informed votes on the thousands of proposals presented annually at meetings of portfolio companies. To ensure they are able to fulfill their fiduciary duties to the Main Street investors who are their beneficiaries, institutional investors often engage proxy voting advisors to assist them in formulating and selecting voting policies in aggregate and to provide company-specific research to apply those policies to make well-informed decisions on individual

[1] In the interest of full disclosure, the Council notes that plaintiff Institutional Shareholder Services Inc. (ISS) and another large proxy advisory firm affected by the SEC action challenged in this suit, Glass Lewis & Co., are non-voting associate members of CII. In aggregate, ISS and Glass Lewis pay annual dues representing less than 1.0% of CII's membership revenues. In addition, CII and several of the additional amici are clients of ISS, Glass Lewis, or both. However, this brief was not authored in whole or in part by counsel for any party, and no person or entity other than amici or their counsel has made a monetary contribution to the preparation or submission of the brief. The views expressed in the brief are those of amici alone.

proxy votes. The critical and independent analysis performed by proxy voting advisors, and the vote recommendations they deliver based on criteria and policies selected and agreed by the clients they advise, efficiently and effectively fulfill a key need for institutional investors and their beneficiaries. Accordingly, amici have a strong interest in ensuring that timely and high-quality independent proxy voting advice remains available in the marketplace and that regulatory actions that threaten the integrity and quality of such advice, like the challenged rule amendments, are not adopted.

ARGUMENT

Proxy advisors effectively and efficiently serve as collective research providers for large numbers of institutional investors, providing an affordable, high-quality alternative to the otherwise-prohibitive cost of analyzing in-house literally hundreds of thousands of ballot proposals at thousands of shareholder meetings each proxy season. The amendments to Rules 14a-1, 14a-2, and 14a-9 challenged here put at serious and unwarranted risk the continued availability of timely, high-quality, and independent advice and analysis of issues subject to shareholder vote.

Institutional investors—the clients of proxy voting advisor firms and supposed principal beneficiaries of the new rules—did not ask for the amendments, do not want them, and do not believe they are needed to facilitate investors' ability to obtain the information necessary to make informed voting decisions. The amendments treat proxy advisors as if they were engaged in proxy solicitation when they are not and then, because they are not, afford advisors an exemption—but only if they satisfy

conditions that will impair their independence and harm investors. In the view of amici, there is no legal or economic basis for that approach.

The Commission failed to provide reliable evidence indicating that the existing proxy advisor communications with their institutional investor clients present a significant risk to investor protection that justifies this regulatory action. The proposed rule amendments were premised in part on an assumed (but never substantiated) rate of factual errors and methodological weaknesses in proxy voting advice that materially impacts shareholder voting decisions. Confronted with evidence disproving that foundational assumption, the Commission refused to engage with that evidence and never questioned whether regulatory intervention was still warranted. To the contrary, it blithely concocted a new justification for its predetermined course of action, ignoring the radical diminution of benefits inherent in shifting goals from avoiding purported material errors in advice to a milquetoast commitment to "fostering dialogue." Its deficient justification for the rule amendments compounds that error twice over, first by discounting the harms to institutional investors and their beneficiaries that will flow from compromising the quality and independence of proxy advisors' analyses and then again by disregarding the serious constitutional concerns created by forcing proxy advisors to disseminate and subsidize issuers' rebuttals of critical voting advice.

As Commissioner Herren Lee rightly observed in her dissent from the vote to adopt them, the rule amendments are "unwarranted, unwanted, and unworkable." Comm'r Allison Herren Lee, *Paying More for Less: Higher Costs for Shareholders,*

Less Accountability for Management (July 22, 2020), https://perma.cc/DF75-YJGP ("Lee Dissent"). Amici agree. The Court should set the Commission's action aside.

I. THE SEC'S DETERMINATION THAT PROXY VOTING ADVICE DELIVERED TO AN INVESTOR REQUESTING THAT ADVICE CONSTITUTES A "SOLICITATION" UNDER SECTION 14(a) IS CONTRARY TO LAW AND ARBITRARY AND CAPRICIOUS.

Amici agree with ISS that proxy voting advice is not a solicitation within the meaning of Section 14(a). *See* 15 U.S.C. §78n(a). A disinterested advisor evaluating and providing advice on matters to be voted by proxy according to criteria agreed between the advisor and investor is not "soliciting" a proxy under any reasonable construction of that term. That conclusion does not change simply because the advisor is paid for its research and analysis or because it markets its advisory services generally. First, the relevant communication—namely, the research and advice provided to the investor—is actively solicited by the investor. Second, the proxy advisor has no interest in the outcome of any proxy vote, whether its advice is vindicated, or even whether that advice is followed. Third, the advisor makes recommendations not based on its own priorities but according to criteria selected or even crafted by the investor in the first instance. Because of these factors, delivering proxy voting advice to a client paying for that advice does not "solicit a[] proxy or consent or authorization," *id.* §78n(a)(1), nor are the circumstances under which proxy voting advice is delivered ones "reasonably calculated to result in the procurement, execution, or revocation of a proxy." 17 C.F.R. §240.14a-1(*l*)(1)(iii).

Irrespective, the SEC's action cannot be sustained because it fails to grapple with the fact that it has changed course significantly by reinterpreting "solicit" to

encompass proxy voting advice. "Agencies are free to change their existing policies as long as they provide a reasoned explanation for the change." *Encino Motorcars, LLC v. Navarro*, 136 S.Ct. 2117, 2125 (2016). But while a regulatory change from an existing position does not always demand "a more detailed justification than what would suffice for a new policy created on a blank slate," the agency "must at least 'display awareness that it is changing position' and 'show that there are good reasons for the new policy.'" *Id.* at 2125-26 (2016) (quoting *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515-16 (2009)). Moreover, the agency must "be cognizant that longstanding policies may have 'engendered serious reliance interests that must be taken into account.'" *Id.* at 2126 (quoting *Fox Television*, 556 U.S. at 516).

An agency's failure to follow these precepts carries consequences. "[A]n 'unexplained inconsistency' in agency policy is 'a reason for holding an interpretation to be an arbitrary and capricious change from agency practice.' An arbitrary and capricious regulation of this sort is itself unlawful and receives no *Chevron* deference." *Encino Motorcars*, 136 S.Ct. at 2126 (quoting *Nat'l Cable & Telecoms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 981 (2005)); *see also Lone Mtn. Processing, Inc. v. Sec'y of Labor*, 709 F.3d 1161, 1164 (D.C. Cir. 2013) ("[A]n agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored.").

There is no room for serious dispute that the rule amendments adopted here constitute a significant change of course. For decades, the SEC has not treated proxy voting advice that investors actively request from proxy advisors as constituting a

solicitation by the proxy advisor—as distinguished from "unsolicited" voting advice, which it has. *See Broker-Dealer Participation in Proxy Solicitations*, Exch. Act Rel. No. 7208, 29 Fed. Reg. 341, 341 (Jan. 15, 1964) (confirming that brokers' proxy voting advice is a solicitation only insofar as they "go[] beyond [their] advisory function" to distribute advice "to persons who have not asked for it," whereas providing such advice "in [their] capacity as adviser to the customer" is not); *Shareholder Comm'cns, Shareholder Participation in the Corporate Electoral Process, and Corporate Governance Generally*, Exch. Act Rel. No. 16356, 44 Fed. Reg. 68764, 68767 n.11 (Nov. 29, 1979) (recognizing that an advisor furnishing proxy voting advice within the context of a fiduciary relationship with an investor is not soliciting a proxy). Now, however, the SEC contends that the considerations that previously *excluded* proxy voting advice from the regulatory regime governing proxy solicitation are the same considerations that now somehow provide the critical factors justifying its inclusion under that regime. *See, e.g.*, *Exemptions from the Proxy Rules for Proxy Voting Advice*, Exch. Act. Rel. No. 34-89372, 85 Fed. Reg. 55082, 55091 & n.124 (Sept. 3, 2020) ("Adopting Release") ("[T]he amendment is intended to apply to entities that market their proxy voting advice as a service that is separate from other forms of investment advice to clients or prospective clients and sell such advice for a fee.").

Far from providing a reasoned justification for its about-face, the SEC simply denies that any change is occurring. *E.g.*, Adopting Release at 55089 ("The proposed amendment would codify the long-held Commission view that the furnishing of proxy voting advice generally constitutes a solicitation governed by the federal proxy

rules."). Its principal support for this claim is a guidance document issued, without notice or comment, just last year and immediately challenged in this suit. But that guidance only parrots the same incorrect assertions concerning the agency's past treatment of proxy voting advice. The SEC cannot elide inconvenient historical facts through disinformation and ipse dixit. *See Am. Wild Horse Preservation Campaign v. Perdue*, 873 F.3d 914, 924 (D.C. Cir. 2017) ("That argument flatly defies the plain text of the official 1991 Forest Plan, repeated official agency statements, and two decades of agency practice. Blinders may work for horses, but they are no good for administrative agencies."). Moreover, the Commission's recent guidance is equally devoid of analysis justifying the significant alteration of the regulatory environment governing proxy voting advice. The agency cannot avoid its obligation to explain its regulatory U-turn through such bootstrapping. *See, e.g.*, Adopting Release at 55132 (refusing to treat pre-guidance status quo as baseline for economic analysis, despite guidance not having conducted its own analysis of costs and benefits). Having previously abdicated its responsibility to explain and justify the agency's departure from its prior regulatory path in the guidance, the SEC cannot justify subsequent actions simply by claiming consistency with that unexplained new policy. "An agency may not depart from a prior policy sub silentio" by degrees any more than it can in a single fell swoop. *Grace v. Barr*, 965 F.3d 883, 898 (D.C. Cir. 2020) (cleaned up).

The SEC's refusal to acknowledge historical reality creates serious and inexcusable deficiencies throughout the agency's analysis. Claiming that proxy voting advice has always been a solicitation, for instance, allows the agency to entirely

ignore the significant costs and counterproductive effect of creating or expanding liability exposure for proxy voting advisors under Rule 14a-9. *E.g.*, Adopting Release at 55095 ("[A]ny impact from codifying this aspect of the definition of a solicitation likely is already reflected in the manner in which proxy voting advice businesses provide their services and the pricing thereof."); *id.* at 55134 ("The Commission is unaware of specific evidence that the interpretation [of 'solicitation'] has resulted or would result in a substantial increase in costs due to the application of Rule 14a-9 to proxy voting advice."). Likewise, the agency never even mentions, much less analyzes, proxy advisors' and investors' reasonable reliance interests representing investments and expectations generated under the decades-long prior policy. *See, e.g.*, *Mozilla Corp. v. FCC*, 940 F.3d 1, 63 (D.C. Cir. 2019) ("The Commission acknowledged, *as it must*, the significance of reliance interests as a potential weight against its decision." (emphasis added)). These omissions, just as much as the failure to acknowledge the change in regulatory treatment imposed by the rule amendments, require setting the amendments aside as arbitrary and capricious.

II. BECAUSE THERE IS NO RELIABLE EVIDENCE OF ACTUAL ERRORS IN PROXY VOTING ADVICE, THE SEC'S ACTION IS UNJUSTIFIED BOTH LEGALLY AND ECONOMICALLY.

The rule amendments are a solution in search of a problem. The Commission began by assuming the prevalence of material errors in proxy voting advice and predicated its proposal to amend the rules on their existence. The Council and other commenters debunked what little evidence there was to support the Commission's presupposition, and the Commission thereafter made no effort to develop an evidentiary record that would justify regulatory action. As a result, the only basis the

SEC has for asserting that the rule amendments will have any benefit at all—or that the rules' very real costs will not outweigh those phantom benefits—is its own say-so. That is not enough.

The agency proposal for amending the proxy rules to govern voting advice was explicitly motivated in part by unsubstantiated allegations from issuers and their advocates of significant rates of factual and analytical errors in proxy voting advice. *See, e.g.*, *Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice*, Exch. Act Rel. No. 34-87457, 84 Fed. Reg. 66518, 66520 (Dec. 4, 2019) ("Proposing Release") ("[W]e are concerned about the risk of proxy voting advice businesses providing inaccurate or incomplete voting advice . . . . In light of these concerns, we are proposing amendments to the federal proxy rules that are designed to enhance the accuracy, transparency of process, and material completeness of the information provided to clients of proxy voting advice businesses."). That key premise underlying the rule amendments is wholly unsupported on the record the SEC had before it.

Even before the Commission issued its proposed rules, it knew that the evidence underlying issuers' claims was unreliable and overstated. In an October 2019 letter to the Commission commenting on the proxy advice guidance, the Council detailed its reanalysis of an American Council on Capital Formation study widely cited by issuer advocates as proving a pervasive pattern of voting advice errors. Letter from CII Exec. Director Kenneth A. Bertsch to SEC Chairman Jay Clayton et al. (Oct. 24, 2019), https://perma.cc/H4Y3-KK47. The Council demonstrated that the ACCF study was riddled with miscategorizations and errors of its own and that, of the 139

purported advice errors alleged over a three-year period, at most 18 represented factual inaccuracies that could be blamed on proxy advisory firms. *Id.* at 2-4. Of the 31,830 reports ISS and Glass Lewis issued during the study period, those 18 instances generated an error rate of 0.057%. *Id.*

The Council repeated the exercise after the Commission's proposing release relied on nose-counting of 2018 supplemental proxy filings that expressed "concerns" about negative voting recommendations. Letter from CII Exec. Director Kenneth A. Bertsch to SEC Secretary Vanessa A. Countryman (Feb. 4, 2020), https://perma.cc/3R8B-N2C3; *see* Proposing Release at 66546 (Table 2). As with the ACCF study, the Council demonstrated that the number of asserted factual or analytical errors was overstated; that the purported analytical errors were actually disagreements on analytic methodology, not errors; that assertions of factual error were actually made in only 7 of 84 identified filings; and that most of those assertions were incorrect. *Id.* at 8-18.[2] The ultimate conclusion—that of more than 11,000 proxy

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[2] First in a November 7, 2019 letter, and in numerous meetings and letters thereafter, CII repeatedly asked the Commission to release the data underlying the number and classification of "concerns" summarized in the Proposing Release's Table 2, including through filing a FOIA request. *See id.* at 6 n.18 (documenting numerous interactions regarding CII's request for the Table 2 data). Seventy days after CII's initial request, and only 18 days before the close of the comment period, the Commission published a staff memo identifying the specific supplemental proxy filings analyzed in Table 2, but it again failed to disclose the key data CII had asked for—which filings were categorized into which error classifications. SEC, Div. of Econ. & Risk Analysis, Memorandum, *Data Analysis of Additional Definitive Proxy Materials Filed by Registrants in Response to Proxy Voting Advice* (Jan. 16, 2020), https://perma.cc/HP2F-T6VU ("DERA Memo"). The memo did acknowledge, however, that its classification judgments were essentially subjective. *See id.* at 1-2, 4 ("Different reviewers may reach different conclusions about the classifications."). CII appealed the FOIA response; after the comment period's close, the SEC's Office of

advisor reports issued in 2018, factual errors occurred in just 0.06%—aligns strikingly with the multi-year error rate obscured in the ACCF study. *See id.* at 11.

That vanishingly small rate of actual errors—as opposed to management disagreements with advisors' use of methodologies that result in unfavorable recommendations—presents a clearly insufficient basis for rulemaking. As Commissioner Herren Lee observed about the proposing release, "[w]hat is missing" are "data demonstrating an error rate in proxy advice sufficient to warrant a rulemaking. In fact, as the comment file shows, assertions of widespread factual errors have been methodically analyzed and largely disproven." Comm'r Allison Herren Lee, *Statement on Shareholder Rights* (Nov. 5, 2019), https://perma.cc/MDQ7-L2PD. That remains true today. *See* Lee Dissent ("[W]e still have not produced any objective evidence of a problem with proxy advisory firms' voting recommendations. No lawsuits, no enforcement cases, no exam findings, and no objective evidence of material error—in nature or number. Nothing.").

Confronted with that thorough debunking of the evidence underpinning its proposal, the Commission offered no response to the exhaustive critiques challenging

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General Counsel found that the Commission had not performed a reasonable search for responsive documents. The requested information still has not been provided.

The Commission's discussion of Table 2 is, at best, misleading. It asserts it "made no judgment as to whether the concerns raised by registrants in their supplemental filings were valid." Adopting Release at 55131. Left unsaid, however, are the ways that it concededly *did* make judgments about registrants' allegations—first by creating subjective categories for classifying registrant "concerns," and second by assigning registrant responses to those categories according to subjective criteria. DERA Memo at 4. By failing to provide the information CII requested, the Commission ensured that the appropriateness of those judgments cannot be fully assessed.

its assumptions regarding "the likelihood of factual errors or methodological weaknesses in proxy voting advice." Proposing Release at 66525. Instead, the Commission has tried to whitewash its dependence on the supposed prevalence of factual errors in voting advice to justify the amendments. But the reality of its continued reliance on allegations of errors bleeds through. *See, e.g.*, Adopting Release at 55084, 55085, 55102, 55108 (reiterating, serially, the proposal's goal of "more transparent, accurate, and complete" voting advice); *id.* at 55091, 55141 (describing aim of "enhancing the quality" and "enhancing the accuracy" of voting advice).

Given its initial—and, apparently, ongoing—reliance on that central justification for regulating proxy voting advice, it is inadequate and fundamentally arbitrary for the Commission to simply state that the purported rate of advice errors was no longer a basis for rulemaking. "Conclusory explanations for matters involving a central factual dispute where there is considerable evidence in conflict do not suffice to meet the deferential standards of [APA] review." *Int'l Union, United Mine Workers of Am. v. Mine Safety & Health Admin.*, 626 F.3d 84, 94 (D.C. Cir. 2010). The Commission's failure to address the fact that a key assumption motivating its regulatory action was contradicted by the evidence establishes that it did not examine all relevant factors in its decision. *See, e.g.*, *Carlson v. Postal Reg. Comm'n*, 938 F.3d 337, 344 (D.C. Cir. 2019) ("An agency also violates [the APA's arbitrary-and-capricious] standard if it fails to respond to 'significant points' and consider 'all relevant factors' raised by the public comments."). After all, merely "[n]odding to concerns raised by commenters only to dismiss them in a conclusory manner is not a

hallmark of reasoned decisionmaking." *Gresham v. Azar*, 950 F.3d 93, 103 (D.C. Cir. 2020).

To the extent the Commission now tries to justify the amendments as furthering the vague goal of "enhancing the overall mix of information available to [proxy advisors'] clients," Adopting Release at 55135, it merely trades one unsupported assumption for another. Management views on issues subject to shareholder votes may be valuable, but these rule amendments assume that those views are, per se, "so valuable we should add cost, complexity, and delay into the process in order to ensure that they are considered. *There is simply no evidence for this premise*." Lee Dissent n.6 (emphasis added). Even more problematic, "the release does not even attempt to make that case." *Id.* The Commission simply assumes "more is better," yet both halves of that equation are deeply suspect.

First, it is unlikely that there will be more issuer input, except to contest negative recommendations. The Commission asserts that issuers "may" respond to voting advice even when it does not conflict with management recommendations, but its own analysis suggests such supposition is no more than a theoretical possibility. *See* Adopting Release at 55139 ("We expect a registrant would bear these costs only if it anticipated the benefits of such steps would exceed the costs of such a program."). In the real world, it is a good bet that—just as is the case now—issuers will prepare supplemental filings only when management disagrees with a negative vote recommendation. The rules do virtually nothing to adjust those incentives,

suggesting that the real point is not to increase issuer input overall, but rather simply to amplify management's voice when disputes with proxy voting advisors arise.

Second, increasing input from only one side does not make for a better-informed debate. The Commission's aim—"improving client access to registrant information and analysis," *id.* at 55131—is curiously selective. If the goal is for shareholders to have more information to contextualize voting advice and make fully informed voting decisions, one might think dissident proposal proponents and other non-management sources would be permitted the same access and right to rebut voting recommendations. But these rule amendments expressly exclude them. *Id.* at 55109 n.338 ("We believe that it could have been unduly burdensome on proxy voting advice businesses to extend the requirements of Rule 14a-2(b)(9)(ii)(A) to other soliciting persons (in addition to the relevant registrants)."). The limitation likewise suggests that the goal of the amendments is not so much to make more information available to voters as it is to increase the portion of that information that reflects issuers' point of view.

As these factors demonstrate, the principal—indeed, potentially the *only*—circumstance in which the rules are likely to operate is to amplify management's voice in circumstances when proxy advisors decline to toe the management line. That is not a valid basis for regulatory action at all. *See Buckley v. Valeo*, 424 U.S. 1, 48-49 (1976) ("[T]he concept that government may restrict the speech of some elements of our society in order to enhance the relative voice of others is wholly foreign to the First Amendment."); *see also Pac. Gas & Elec. Co. v. Pub. Utils. Comm'n of Cal.*, 475

U.S. 1, 13 (1986) (*PG&E*) ("Access is limited to persons or groups—such as TURN—who disagree with appellant's views . . . . Such one-sidedness impermissibly burdens appellant's own expression.").

As against these phantom benefits, the rules impose serious and very real costs, both on advisors and investors. The amendments could delay the dissemination of advice to investors, further reducing the limited time they have to factor it into well-considered voting decisions. The regulatory requirements to ensure at least concurrent distribution of advice to issuers and to guarantee distribution of rebuttal information to clients will undoubtedly increase proxy advisors' internal costs, Adopting Release at 55136, and those costs will inevitably be passed along to institutional-investor clients (and, thus, their beneficiaries) "through higher fees for proxy advice," *id.* at 55139. And those costs are insignificant compared to the risk that the rules will compromise the integrity and independence of proxy voting advice, robbing investors of the opportunity to seek critical opinions on matters up for votes. *See* Part III *infra*.

The reality here is that issuers and their advocates want to rein in independent advice that assists shareholders in holding management to account. Institutional investors pay for voting advice from proxy advisors precisely because they are independent from management and thus able to report objectively and critically on executive compensation plans, director qualifications and independence, and other issues informing shareholder votes. As the SEC's own Investor Advocate put it, "the simple fact of the matter seems to be that proxy advisors have given asset managers

an efficient way to exercise much closer oversight of the companies in their portfolios, and those companies don't like it." Rick Fleming, Speech, *Important Issues for Investors in 2019*, at The SEC Speaks in 2019 (Apr. 8, 2019), https://perma.cc/HZ2N-47GZ. It is unsurprising that companies and management executives do not always welcome critical evaluations generated through analytical frameworks different from their own. But critical analysis is not automatically erroneous analysis—far from it. And absent any reliable evidence that factual errors or methodological weaknesses in proxy voting advice are actually prevalent and material at rates sufficient to impact voting recommendations, there is no economic or legal justification for the SEC to mandate rules that damage the integrity and quality of proxy voting advice and harm the investors that employ it.

III. Interfering with the Independence of Proxy Voting Advice Disserves the Commission's Stated Goals and Harms Investors.

Amici are deeply concerned that subjecting proxy voting advice to the burdensome regulatory framework adopted by the Commission will impair the independence of proxy advisors, reducing the reliability and completeness of voting advice. Such an outcome will both impede the achievement of the Commission's aim and harm investors.

The Commission claims that revising the proposed rules to eliminate the requirement of pre-publication issuer review of voting advice obviates these concerns. But as the dissenting commissioner observed, "[t]his is simply not so." Lee Dissent. Substituting the most obnoxious feature of the proposed rule amendments with a moderately less onerous version does not eliminate the risk to proxy advisors'

independence. Particularly as pre-dissemination review is still "encouraged to the extent feasible," Adopting Release at 55109, it is deeply disingenuous for the Commission to assert that "the rule does not create the risk that such advice would be delayed or that the independence thereof would be tainted as a result of a registrant's pre-dissemination involvement." *Id.* at 55112.[3]

Even if the risk of direct interference is lower because issuers' involvement in finalizing advice for publication is merely encouraged, rather than required, other pressures generated by the rule amendments could diminish proxy advisors' willingness to recommend votes against management and reduce the amount of robust, independent analysis available to investors. *See* Nicolas Grabar et al., *The SEC Takes Action on Proxy Advisory Firms*, Harv. Law Sch. Forum on Corp. Governance (Aug. 19, 2020), https://perma.cc/AF2K-2U5C ("The new framework . . . may make the proxy advisory firms more open to adjusting their advice."). In particular, the Commission repeatedly refused to account for the cost of self-censorship by proxy voting advisors likely to result from exposing them to new or

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[3] Commission-approved rules ban prior review of financial analysts' reports by subject companies in order to safeguard the analysts' independence and integrity. *See* FINRA Rule 2241(b). Given the universal recognition that proxy advisors' role is "comparable" to that of financial analysts, Chairman Jay Clayton, *Statement at Open Meeting* (Nov. 5, 2020), https://perma.cc/H3GQ-3NK4, amici note that it is no less critical to protect their work from interference and that there is little difference in potential for corroding analyst independence between, on the one hand, issuers' prior review of proxy advisors' analysis and recommendations and, on the other, companies' prior review of independent financial analysis and opinions. In both instances, facilitating management's rebuttals of statements they dislike negatively impacts the independence, and thus the integrity, of the analysis. The Commission should have justified, but never has, why it not only allows but affirmatively encourages something that rules it enforces would make illegal if done by a financial analyst.

increased liability to issuers for alleged misstatements or omissions in proxy advice under Rule 14a-9. Adopting Release at 55140, 55141; *see* 17 C.F.R. §240.14a-9. It did so notwithstanding its not-so-tacit recognition that such self-censorship is entirely foreseeable. *See, e.g.*, Adopting Release at 55121 ("[T]he lack of legal certainty could affect the quality of analyses by proxy voting advice businesses."); *id.* at 55132 ("To the extent that some proxy voting advice businesses did not previously understand their voting advice to constitute solicitations and thus be subject to Rule 14a-9 liability, it is possible that this heightened awareness could cause those businesses to take more care in preparing their recommendations.").

Courts have long understood that, "[w]here a prosecution is a likely possibility, . . . speakers may self-censor rather than risk the perils of trial." *Ashcroft v. Am. Civil Liberties Union*, 542 U.S. 656, 670-71 (2004). As the D.C. Circuit observed in the analogous context of newspapers' potential libel liability for criticizing public officials:

> The threat of being put to the defense of a lawsuit . . . may be as chilling to the exercise of First Amendment freedoms as fear of the outcome of the lawsuit itself, especially to advocates of unpopular causes. . . . Unless persons, including newspapers, desiring to exercise their First Amendment rights are assured freedom from the harassment of lawsuits, they will tend to become self-censors. And to this extent debate on public issues and the conduct of public officials will become less uninhibited, less robust, and less wide-open, for self-censorship affecting the whole public is hardly less virulent for being privately administered.

Wash. Post Co. v. Keogh, 365 F.2d 965, 968 (D.C. Cir. 1966) (internal quotation marks omitted). Because that dynamic creates the "potential for extraordinary harm and a serious chill upon protected speech," *Ashcroft*, 542 U.S. at 671, the government "should be hesitant to impose responsibilities . . . which can be met only through costly procedures or through self-censorship designed to avoid the risks of publishing

controversial material." *Keogh*, 365 F.2d at 972. The Commission's damn-the-torpedoes determination to see these rules adopted flunks that test.

Here, the rules' chilling effect on proxy advisors clearly disserves the Commission's ostensible goal of providing investors a "robust discussion of views." Adopting Release at 55123. Likewise, it violates the Exchange Act's statutory prohibition against rules that impose an unnecessary or inappropriate burden on competition. 15 U.S.C. §78w(a)(2); *cf. Keogh*, 365 F.2d at 968, 972 ("The costliness of this process would especially deter less established publishers from taking chances, and . . . competition with publishers who can afford to verify or to litigate would become even more difficult."). Yet the Commission discounts those negative effects out of hand, refusing to give them any weight whatsoever in its analysis. *See* Adopting Release at 55140-41 (dismissing concerns that application of Rule 14a-9 liability would "result in a shift to more pro-registrant proxy voting recommendations," "would have a silencing effect on proxy voting advice businesses," or "could reduce the independence of proxy voting advice businesses and the diversity of thought in the market for proxy advice" because the amendments purportedly "do[] not change the scope or application of existing law").[4] This is a classic example of an agency "fail[ing] to respond to significant points and consider all relevant factors raised by the public

[4] Relatedly, the Commission never addressed the Council's comments suggesting the establishment of a Rule 14a-9 safe harbor for proxy advisors satisfying the amendments' procedural requirements in order to lessen these concerns. That unfortunate omission deprives the Court of any explanation from the Commission for its apparent view that the benefit of leaving Rule 14a-9 liability hanging over the heads of proxy advisors, despite the absence of evidence of material errors in their advice, outweighs the cost of the self-censorship that is likely to result.

comments." *Carlson*, 938 F.3d at 344. As a result, the Commission acted in an arbitrary and capricious fashion, and the amendments should be set aside.

IV. FORCING PROXY ADVISORS TO DISSEMINATE ISSUERS' CONTRARY VIEWS VIOLATES THE FIRST AMENDMENT.

The unconstitutionality of forcing a publication to grant the subjects of its criticism a "right of reply" is a long-settled issue. *Miami Herald Pub. Co. v. Tornillo*, 418 U.S. 241 (1974). The parallels to *Tornillo* here are many, and plain—the assertion that "the power to inform . . . and shape public opinion" is limited to a purported monopoly of editorializing speakers, with accusations of resulting "abuses of bias and manipulative reportage"; the claim that the "government has an obligation to ensure that a wide variety of views reach the public"; the proposition that "the only effective way to insure fairness and accuracy and to provide for some accountability is for government to take affirmative action"; the selected remedy of a prescribed "right to reply" to criticism and force its distribution to an interested audience. *Id.* at 247-48, 250-51. But though a "responsible press is an undoubtedly desirable goal," "press responsibility is not mandated by the Constitution and like many other virtues it cannot be legislated." *Id.* at 256. Rather, any "compulsion exerted by government on a newspaper . . . to publish that which reason tells them should not be published is unconstitutional." *Id.* So too with proxy voting advice.

The fact of that First Amendment violation is not ameliorated simply because the rule amendments mandate distribution of a link to issuers' supplemental filings, rather than including such responses within their own voting recommendation reports. Just as the "constitutional difficulty with the right-of-reply statute [in

Tornillo] was that it required the newspaper to disseminate a message with which the newspaper disagreed," *PG&E*, 475 U.S. at 18, proxy advisors are forced by the Commission's new rules to disseminate issuers' rebuttals to their clients. It is irrelevant, constitutionally, that those responses appear via issuers' own filings: "This difficulty did not depend on whether the particular paper on which the replies were printed belonged to the newspaper or to the candidate." *Id*. And just as the California PUC's order in *PG&E* did not "require [the utility] to place TURN's message in [its] newsletter," but was nonetheless unconstitutional because it required PG&E "to carry speech with which it disagreed, and might well feel compelled to reply or limit its own speech in response," *id.* at 12 n.7, the rule amendments mandate that proxy advisors disseminate to their clients issuers' rebuttals of their own advice and analysis, which may prompt those advisors to reply after the fact or refrain from making controversial statements in the first place. Either way, the rules' effect is impermissible. "That kind of forced response is antithetical to the free discussion that the First Amendment seeks to foster." *Id.* at 16. "[W]hen dissemination of a view contrary to one's own is forced upon a speaker intimately connected with the communication advanced, the speaker's right to autonomy over the message is compromised" and the First Amendment violated. *Hurley v. Irish-Am. Gay, Lesbian & Bisexual Group of Boston*, 515 U.S. 557, 576 (1995). That is precisely what these rules demand.

The Commission compounds the constitutional problems inherent in its approach by requiring proxy advisors, in order to come within the safe-harbor

exemption from the proxy filing rules, not simply to disseminate issuers' speech but also to *subsidize* that speech. "Because the compelled subsidization of private speech seriously impinges on First Amendment rights, it cannot be casually allowed." *Janus v. Am. Fed'n of State, Cnty., & Mun. Employees, Council 31*, 138 S.Ct. 2448, 2464 (2018). The Commission, though, embraces compulsory subsidies not just casually, but determinedly: "For purposes of the safe harbor, we believe that the benefit to investors of more timely, complete, and reliable information should not be lessened by making a registrant's ability to review proxy voting advice dependent on the registrant's willingness to pay for it." Adopting Release at 55110 n.347; *see also id.* at 55139 n.622 (acknowledging that conditioning the safe harbor on free access for issuers might cause proxy advisors "to lose fees they otherwise would have earned from selling proxy voting reports to registrants"). And to the extent that the rule amendments permit proxy advisors to charge issuers while still falling within the "principles-based requirements" of the filing exemption, they can only charge fees a court might subsequently deem "reasonable" under the facts and circumstances, not whatever the market may bear, and that only up to "the extent [at] which such fees may dissuade a registrant from seeking to review and provide a response to such proxy voting advice." *Id.* at 55115. Thus, even outside the safe harbor, the rule amendments force proxy advisors to subsidize some, if not all, of the issuers' costs for speaking. The First Amendment does not permit the Commission to make that choice. *See Janus*, 138 S.Ct. at 2464 ("As Jefferson famously put it, 'to compel a man to furnish contributions of money for the propagation of opinions which he disbelieves

and abhors is sinful and tyrannical.'" (quoting 2 PAPERS OF THOMAS JEFFERSON 545 (J. Boyd ed. 1950); alteration omitted)).

There is no possibility of these rules surviving First Amendment review, no matter the degree of scrutiny applied.[5] Even under even the laxest of the potentially applicable standards, a regulation "still must be 'narrowly tailored to serve a significant governmental interest.'" *McCullen v. Coakley*, 574 U.S. 464, 486 (2014) (quoting *Ward v. Rock Against Racism*, 491 U.S. 781, 796, 799 (1989)). These rules fail that narrow-tailoring requirement—and so, necessarily, also fail the more strenuous tailoring demanded by exacting or strict scrutiny—because, as the adopting release itself documents, significantly less speech-restrictive means are unquestionably available to issuers to put their responses to proxy voting advice before investors. "Whether or not proxy voting advice businesses permit registrants to review draft proxy voting advice, all registrants are able to respond to final proxy voting advice by filing additional definitive proxy materials." Adopting Release at 55130. And while the Commission believes it may "be difficult" for issuers to file such materials before investors' votes are first cast, "shareholders have the ability to change their vote at any time prior to a meeting, including as a result of a registrant filing supplemental proxy materials in response to proxy voting advice." *Id.* at 55130

[5] Amici agree with ISS that strict scrutiny of the rule amendments is warranted, both because of their compelled-speech aspects, *see Turner Broad. Sys., Inc. v. FCC*, 512 U.S. 622, 642 (1994), and because of the blatant preference for management voices embedded in their design and operation, *see City of Ladue v. Gilleo*, 512 U.S. 43, 51-52 (1994) (noting that "a compelling justification" is necessary when a law "represent[s] a governmental attempt to give one side of a debatable public question an advantage in expressing its views to the people").

& n.552. Perhaps the Commission's rules would make responding to proxy advice more efficient for issuers, but "the First Amendment does not permit the State to sacrifice speech for efficiency." *Riley v. Nat'l Fed'n of the Blind of N.C., Inc.*, 487 U.S. 781, 795 (1988).

The SEC previously recognized and respected the serious First Amendment implications of a regulatory approach like that adopted here:

> A regulatory scheme that inserted the Commission staff and corporate management into every exchange and conversation among shareholders, their advisors and other parties on matters subject to a vote certainly would raise serious questions under the free speech clause of the First Amendment, particularly where no proxy authority is being solicited by such persons. This is especially true where such intrusion is not necessary to achieve the goals of the federal securities laws.

Regulation of Commc'ns Among Shareholders, Exch. Act Rel. No. 34-31326, 57 Fed. Reg. 48276, 48279 (Oct. 22, 1992). The Commission was right then; it is wrong now. The Court should vacate the rule amendments' adoption and enjoin any future enforcement.

CONCLUSION

For these reasons, amici curiae the Council of Institutional Investors et al. respectfully request that the Court hold the SEC's amendments to Rules 14a-1, 14a-2(b), and 14a-9 to be contrary to law and arbitrary and capricious and set aside their adoption pursuant to 5 U.S.C. §706.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that, on the 9th day of October, 2020, I served a copy of the foregoing Brief Amici Curiae on the attorneys of record for all parties via the Court's electronic filing system.

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The California Public Employees' Retirement System (CalPERS) is the nation's largest defined benefit public pension fund with $411 billion in assets under management as of October 6, 2020. As the nation's largest pension fund, our mission is to deliver retirement and health care benefits for over 2 million CalPERS members and their beneficiaries. For more information about CalPERS, please visit https://www.calpers.ca.gov/page/home.

The California State Controller is Ms. Betty T. Yee. With 35 years of experience in public service, Ms. Yee has served as State Controller since 2015, following two terms on the California Board of Equalization. As the state's chief fiscal officer, she serves on the Board of Equalization, the Franchise Tax Board, the State Lands Commission, the boards for the California Public Employees' Retirement System and California State Teachers' Retirement System, and dozens of other government authorities.

The California State Teachers' Retirement System (CalSTRS) provides a secure retirement to more than 964,000 members whose CalSTRS-covered service is not eligible for Social Security participation. Members retire on average after more than 24 years in the classroom with a monthly benefit of approximately $4,547. Established in 1913, CalSTRS is the largest educator-only pension fund in the world with approximately $262.5 billion in assets under management as of August 31, 2020. CalSTRS demonstrates its strong commitment to long-term corporate sustainability principles in its annual Global Reporting Initiative Sustainability Report. For more information, visit CalSTRS.com.

CFA Institute, a global, not-for-profit organization, is the world's largest association of investment professionals. CFA Institute membership includes more than 185,400 investment analysts, advisers, portfolio managers, and other investment professionals in 163 countries, of whom more than 178,500 hold the Chartered Financial Analyst® (CFA®) designation. CFA Institute's mission is to lead the investment profession globally by promoting the highest standards of ethics, education, and professional excellence for the ultimate benefit of society. CFA Institute builds market integrity for the benefit of society by improving both investor protections and investor outcomes through advocacy work on the topics of capital markets policy, financial reporting policy and systemic risk mitigation. CFA Institute regularly advocates on these topics before regulators around the globe and stands as a respected source of authority in the global financial community. CFA Institute membership includes professional analysts, who have strict and well-regarded professional standards that protect independent analysis by prohibiting undue issuer influences seeking to direct or change the independent research, analysis and opinions of the analyst. We see the SEC's proposal as a threat to analyst independence and the overall integrity of the market.

The Colorado Public Employees' Retirement Association (PERA) is the state's largest public pension plan. We manage approximately $50 billion in assets under statutory fiduciary obligation to enhance the retirement security of more than 600,000 current and former public employees and their beneficiaries. We believe the shareholder right to vote by proxy is, in itself, an asset of the pension plan, and

therefore the prudent management of that right falls within the fiduciary duty owed to the PERA membership. As such, we vote by proxy for shares of domestic and international stocks held in all public equities portfolios within the defined benefit and capital accumulation plans within the Fund, under guidelines set forth by the PERA Board of Trustees. In order to effectively vote proposals in a cost-efficient manner, PERA contracts with proxy advisory firms to obtain access to their objective research and recommendations, and to utilize their vote submission platforms and voting analytics. Although we value and incorporate research from proxy advisors into our analysis, we ultimately vote according to our own guidelines and policies, which we believe are in the best interests of our plan beneficiaries.

The Comptroller of the City of New York is the investment advisor to the five New York City Retirement Systems (NYCRS), which had $222 billion in assets under management as of July 31, 2020. The Comptroller, through its Corporate Governance and Responsible Investment team, is responsible for casting proxy votes at NYCRS' portfolio companies consistent with NYCRS' proxy voting guidelines. For the year ending June 30, 2020, the Comptroller voted on 127,638 individual ballot items at 13,230 shareholder meetings in 84 markets globally, including 26,010 individual ballot items at 3,023 annual and special meetings for U.S. portfolio companies. The Comptroller's ability to faithfully apply NYCRS' proxy voting guidelines rests in large part on the timely receipt of independent, expert research from contracted proxy advisory firms, including ISS.

The CtW Investment Group, **a part of Change to Win,** holds directors accountable for irresponsible and unethical corporate behavior by organizing workers' capital into an effective voice for accountability and retirement security. The Investment Group works with pension funds sponsored by unions affiliated with Change to Win, a federation of unions representing nearly five million members, to enhance long-term shareholder returns through active ownership. The funds CtW works with have about $250 billion assets under management.

The Los Angeles County Employees Retirement Association (LACERA) manages approximately $63 billion in assets in a defined benefit retirement fund and other post-employment benefits. LACERA is the largest county retirement system in the United States. LACERA's mission is to produce, protect, and provide the promised benefits to over 180,000 active and retired members and beneficiaries who are, or have served as, public servants for the County of Los Angeles and other participating employers. LACERA supports sound corporate governance practices and financial market policies that are conducive to generating sustainable financial performance in fulfillment of its mission.