

114TH CONGRESS
2D SESSION

H. R. 5311

To improve the quality of proxy advisory firms for the protection of investors and the U.S. economy, and in the public interest, by fostering accountability, transparency, responsiveness, and competition in the proxy advisory firm industry.

IN THE HOUSE OF REPRESENTATIVES

MAY 24, 2016

Mr. DUFFY (for himself and Mr. CARNEY) introduced the following bill; which was referred to the Committee on Financial Services

A BILL

To improve the quality of proxy advisory firms for the protection of investors and the U.S. economy, and in the public interest, by fostering accountability, transparency, responsiveness, and competition in the proxy advisory firm industry.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Corporate Governance
5 Reform and Transparency Act of 2016”.

1 **SEC. 2. DEFINITIONS.**

2 (a) SECURITIES EXCHANGE ACT OF 1934.—Section
3 3(a) of the Securities Exchange Act of 1934 (15 U.S.C.
4 78c(a)) is amended by adding at the end the following new
5 paragraphs:

6 “(81) PROXY ADVISORY FIRM.—The term
7 ‘proxy advisory firm’ means any person registered
8 under section 15H who is engaged in the business
9 of providing proxy voting research, analysis, or rec-
10 ommendations to clients, which conduct constitutes
11 a solicitation within the meaning of section 14 and
12 the Commission’s rules and regulations thereunder,
13 except to the extent that the person is exempted by
14 such rules and regulations from requirements other-
15 wise applicable to persons engaged in a solicitation.

16 “(82) PERSON ASSOCIATED WITH A PROXY AD-
17 VISORY FIRM.—The term ‘person associated with’ a
18 proxy advisory firm means any partner, officer, or
19 director of a proxy advisory firm (or any person oc-
20 cupying a similar status or performing similar func-
21 tions), any person directly or indirectly controlling,
22 controlled by, or under common control with a proxy
23 advisory firm, or any employee of a proxy advisory
24 firm, except that persons associated with a proxy ad-
25 visory firm whose functions are clerical or ministe-
26 rial shall not be included in the meaning of such

1 term. The Commission may by rules and regulations
2 classify, for purposes or any portion or portions of
3 this Act, persons, including employees controlled by
4 a proxy advisory firm.”.

5 (b) APPLICABLE DEFINITIONS.—As used in this
6 Act—

7 (1) the term “Commission” means the Securi-
8 ties and Exchange Commission; and

9 (2) the term “proxy advisory firm” has the
10 same meaning as in section 3(a)(81) of the Securi-
11 ties Exchange Act of 1934, as added by this Act.

12 **SEC. 3. REGISTRATION OF PROXY ADVISORY FIRMS.**

13 (a) AMENDMENT.—The Securities Exchange Act of
14 1934 is amended by inserting after section 15G the fol-
15 lowing new section:

16 **“SEC. 15H. REGISTRATION OF PROXY ADVISORY FIRMS.**

17 “(a) CONDUCT PROHIBITED.—It shall be unlawful
18 for a proxy advisory firm to make use of the mails or any
19 means or instrumentality of interstate commerce to pro-
20 vide proxy voting research, analysis, or recommendations
21 to any client, unless such proxy advisory firm is registered
22 under this section.

23 “(b) REGISTRATION PROCEDURES.—

24 “(1) APPLICATION FOR REGISTRATION.—

1 “(A) IN GENERAL.—A proxy advisory firm
2 must file with the Commission an application
3 for registration, in such form as the Commis-
4 sion shall require, by rule or regulation, and
5 containing the information described in sub-
6 paragraph (B).

7 “(B) REQUIRED INFORMATION.—An appli-
8 cation for registration under this section shall
9 contain information regarding—

10 “(i) a certification that the applicant
11 has adequate financial and managerial re-
12 sources to consistently provide proxy advice
13 based on accurate information;

14 “(ii) the procedures and methodolo-
15 gies that the applicant uses in developing
16 proxy voting recommendations, including
17 whether and how the applicant considers
18 the size of a company when making proxy
19 voting recommendations;

20 “(iii) the organizational structure of
21 the applicant;

22 “(iv) whether or not the applicant has
23 in effect a code of ethics, and if not, the
24 reasons therefor;

1 “(v) any potential or actual conflict of
2 interest relating to the ownership structure
3 of the applicant or the provision of proxy
4 advisory services by the applicant, includ-
5 ing whether the proxy advisory firm en-
6 gages in services ancillary to the provision
7 of proxy advisory services such as con-
8 sulting services for corporate issuers, and
9 if so the revenues derived therefrom;

10 “(vi) the policies and procedures in
11 place to manage conflicts of interest under
12 subsection (f); and

13 “(vii) any other information and docu-
14 ments concerning the applicant and any
15 person associated with such applicant as
16 the Commission, by rule, may prescribe as
17 necessary or appropriate in the public in-
18 terest or for the protection of investors.

19 “(2) REVIEW OF APPLICATION.—

20 “(A) INITIAL DETERMINATION.—Not later
21 than 90 days after the date on which the appli-
22 cation for registration is filed with the Commis-
23 sion under paragraph (1) (or within such longer
24 period as to which the applicant consents) the
25 Commission shall—

1 “(i) by order, grant registration; or

2 “(ii) institute proceedings to deter-
3 mine whether registration should be de-
4 nied.

5 “(B) CONDUCT OF PROCEEDINGS.—

6 “(i) CONTENT.—Proceedings referred
7 to in subparagraph (A)(ii) shall—

8 “(I) include notice of the grounds
9 for denial under consideration and an
10 opportunity for hearing; and

11 “(II) be concluded not later than
12 120 days after the date on which the
13 application for registration is filed
14 with the Commission under paragraph
15 (1).

16 “(ii) DETERMINATION.—At the con-
17 clusion of such proceedings, the Commis-
18 sion, by order, shall grant or deny such ap-
19 plication for registration.

20 “(iii) EXTENSION AUTHORIZED.—The
21 Commission may extend the time for con-
22 clusion of such proceedings for not longer
23 than 90 days, if it finds good cause for
24 such extension and publishes its reasons

1 for so finding, or for such longer period as
2 to which the applicant consents.

3 “(C) GROUNDS FOR DECISION.—The Com-
4 mission shall grant registration under this sub-
5 section—

6 “(i) if the Commission finds that the
7 requirements of this section are satisfied;
8 and

9 “(ii) unless the Commission finds (in
10 which case the Commission shall deny such
11 registration) that—

12 “(I) the applicant has failed to
13 certify to the Commission’s satisfac-
14 tion that it has adequate financial and
15 managerial resources to consistently
16 provide proxy advice based on accu-
17 rate information and to materially
18 comply with the procedures and meth-
19 odologies disclosed under paragraph
20 (1)(B) and with subsections (f) and
21 (g); or

22 “(II) if the applicant were so reg-
23 istered, its registration would be sub-
24 ject to suspension or revocation under
25 subsection (e).

1 “(3) PUBLIC AVAILABILITY OF INFORMATION.—
2 Subject to section 24, the Commission shall make
3 the information and documents submitted to the
4 Commission by a proxy advisory firm in its com-
5 pleted application for registration, or in any amend-
6 ment submitted under paragraph (1) or (2) of sub-
7 section (e), publicly available on the Commission’s
8 website, or through another comparable, readily ac-
9 cessible means.

10 “(c) UPDATE OF REGISTRATION.—

11 “(1) UPDATE.—Each registered proxy advisory
12 firm shall promptly amend and update its applica-
13 tion for registration under this section if any infor-
14 mation or document provided therein becomes mate-
15 rially inaccurate, except that a registered proxy advi-
16 sory firm is not required to amend the information
17 required to be filed under subsection (b)(1)(B)(i) by
18 filing information under this paragraph, but shall
19 amend such information in the annual submission of
20 the organization under paragraph (2) of this sub-
21 section.

22 “(2) CERTIFICATION.—Not later than 90 cal-
23 endar days after the end of each calendar year, each
24 registered proxy advisory firm shall file with the
25 Commission an amendment to its registration, in

1 such form as the Commission, by rule, may prescribe
2 as necessary or appropriate in the public interest or
3 for the protection of investors—

4 “(A) certifying that the information and
5 documents in the application for registration of
6 such registered proxy advisory firm continue to
7 be accurate in all material respects; and

8 “(B) listing any material change that oc-
9 curred to such information or documents during
10 the previous calendar year.

11 “(d) CENSURE, DENIAL, OR SUSPENSION OF REG-
12 ISTRATION; NOTICE AND HEARING.—The Commission, by
13 order, shall censure, place limitations on the activities,
14 functions, or operations of, suspend for a period not ex-
15 ceeding 12 months, or revoke the registration of any reg-
16 istered proxy advisory firm if the Commission finds, on
17 the record after notice and opportunity for hearing, that
18 such censure, placing of limitations, suspension, or revoca-
19 tion is necessary for the protection of investors and in the
20 public interest and that such registered proxy advisory
21 firm, or any person associated with such an organization,
22 whether prior to or subsequent to becoming so associ-
23 ated—

24 “(1) has committed or omitted any act, or is
25 subject to an order or finding, enumerated in sub-

1 paragraph (A), (D), (E), (H), or (G) of section
2 15(b)(4), has been convicted of any offense specified
3 in section 15(b)(4)(B), or is enjoined from any ac-
4 tion, conduct, or practice specified in subparagraph
5 (C) of section 15(b)(4), during the 10-year period
6 preceding the date of commencement of the pro-
7 ceedings under this subsection, or at any time there-
8 after;

9 “(2) has been convicted during the 10-year pe-
10 riod preceding the date on which an application for
11 registration is filed with the Commission under this
12 section, or at any time thereafter, of—

13 “(A) any crime that is punishable by im-
14 prisonment for one or more years, and that is
15 not described in section 15(b)(4)(B); or

16 “(B) a substantially equivalent crime by a
17 foreign court of competent jurisdiction;

18 “(3) is subject to any order of the Commission
19 barring or suspending the right of the person to be
20 associated with a registered proxy advisory firm;

21 “(4) fails to furnish the certifications required
22 under subsections (b)(2)(C)(ii)(I) and (c)(2);

23 “(5) has engaged in one or more prohibited acts
24 enumerated in paragraph (1); or

1 “(6) fails to maintain adequate financial and
2 managerial resources to consistently offer advisory
3 services with integrity, including by failing to comply
4 with subsections (f) or (g).

5 “(e) TERMINATION OF REGISTRATION.—

6 “(1) VOLUNTARY WITHDRAWAL.—A registered
7 proxy advisory firm may, upon such terms and con-
8 ditions as the Commission may establish as nec-
9 essary in the public interest or for the protection of
10 investors, which terms and conditions shall include
11 at a minimum that the registered proxy advisory
12 firm will no longer conduct such activities as to
13 bring it within the definition of proxy advisory firm
14 in section 3(a)(81) of the Exchange Act, withdraw
15 from registration by filing a written notice of with-
16 drawal to the Commission.

17 “(2) COMMISSION AUTHORITY.—In addition to
18 any other authority of the Commission under this
19 title, if the Commission finds that a registered proxy
20 advisory firm is no longer in existence or has ceased
21 to do business as a proxy advisory firm, the Com-
22 mission, by order, shall cancel the registration under
23 this section of such registered proxy advisory firm.

24 “(f) MANAGEMENT OF CONFLICTS OF INTEREST.—

1 “(1) ORGANIZATION POLICIES AND PROCE-
2 DURES.—Each registered proxy advisory firm shall
3 establish, maintain, and enforce written policies and
4 procedures reasonably designed, taking into consid-
5 eration the nature of the business of such registered
6 proxy advisory firm and associated persons, to ad-
7 dress and manage any conflicts of interest that can
8 arise from such business.

9 “(2) COMMISSION AUTHORITY.—The Commis-
10 sion shall issue final rules to prohibit, or require the
11 management and disclosure of, any conflicts of inter-
12 est relating to the offering of proxy advisory services
13 by a registered proxy advisory firm, including, with-
14 out limitation, conflicts of interest relating to—

15 “(A) the manner in which a registered
16 proxy advisory firm is compensated by the cli-
17 ent, or any affiliate of the client, for providing
18 proxy advisory services;

19 “(B) the provision of consulting, advisory,
20 or other services by a registered proxy advisory
21 firm, or any person associated with such reg-
22 istered proxy advisory firm, to the client;

23 “(C) business relationships, ownership in-
24 terests, or any other financial or personal inter-
25 ests between a registered proxy advisory firm,

1 or any person associated with such registered
2 proxy advisory firm, and any client, or any af-
3 filiate of such client;

4 “(D) transparency around the formulation
5 of proxy voting policies;

6 “(E) the execution of proxy votes if such
7 votes are based upon recommendations made by
8 the proxy advisory firm in which someone other
9 than the issuer is a proponent;

10 “(F) issuing recommendations where proxy
11 advisory firms provide advisory services to a
12 company; and

13 “(G) any other potential conflict of inter-
14 est, as the Commission deems necessary or ap-
15 propriate in the public interest or for the pro-
16 tection of investors.

17 “(g) RELIABILITY OF PROXY ADVISORY FIRM SERV-
18 ICES.—Each registered proxy advisory firm shall have
19 staff sufficient to produce proxy voting recommendations
20 that are based on accurate and current information. Each
21 registered proxy advisory firm shall detail procedures suf-
22 ficient to permit companies receiving proxy advisory firm
23 recommendations access in a reasonable time to the draft
24 recommendations, with an opportunity to provide mean-
25 ingful comment thereon, including the opportunity to

1 present details to the person(s) responsible for developing
2 the recommendation in person or telephonically. Each reg-
3 istered proxy advisory firm shall employ an ombudsman
4 to receive complaints about the accuracy of voting infor-
5 mation used in making recommendations from the sub-
6 jects of the proxy advisory firm’s voting recommendations,
7 and shall resolve those complaints in a timely fashion and
8 in any event prior to voting on the matter to which the
9 recommendation relates.

10 “(h) DESIGNATION OF COMPLIANCE OFFICER.—

11 Each registered proxy advisory firm shall designate an in-
12 dividual responsible for administering the policies and pro-
13 cedures that are required to be established pursuant to
14 subsections (f) and (g), and for ensuring compliance with
15 the securities laws and the rules and regulations there-
16 under, including those promulgated by the Commission
17 pursuant to this section.

18 “(i) PROHIBITED CONDUCT.—

19 “(1) PROHIBITED ACTS AND PRACTICES.—The
20 Commission shall issue final rules to prohibit any
21 act or practice relating to the offering of proxy advi-
22 sory services by a registered proxy advisory firm
23 that the Commission determines to be unfair, coer-
24 cive, or abusive, including any act or practice relat-
25 ing to—

1 “(A) conditioning a voting recommendation
2 or other proxy advisory firm recommendation
3 on the purchase by an issuer or an affiliate
4 thereof of other services or products, of the reg-
5 istered proxy advisory firm or any person asso-
6 ciated with such registered proxy advisory firm;
7 and

8 “(B) modifying a voting recommendation
9 or otherwise departing from its adopted system-
10 atic procedures and methodologies in the provi-
11 sion of proxy advisory services, based on wheth-
12 er an issuer, or affiliate thereof, subscribes or
13 will subscribe to other services or product of the
14 registered proxy advisory firm or any person as-
15 sociated with such organization.

16 “(2) RULE OF CONSTRUCTION.—Nothing in
17 paragraph (1), or in any rules or regulations adopt-
18 ed thereunder, may be construed to modify, impair,
19 or supersede the operation of any of the antitrust
20 laws (as defined in the first section of the Clayton
21 Act, except that such term includes section 5 of the
22 Federal Trade Commission Act, to the extent that
23 such section 5 applies to unfair methods of competi-
24 tion).

1 “(j) STATEMENTS OF FINANCIAL CONDITION.—Each
2 registered proxy advisory firm shall, on a confidential
3 basis, file with the Commission, at intervals determined
4 by the Commission, such financial statements, certified (if
5 required by the rules or regulations of the Commission)
6 by an independent public auditor, and information con-
7 cerning its financial condition, as the Commission, by rule,
8 may prescribe as necessary or appropriate in the public
9 interest or for the protection of investors.

10 “(k) ANNUAL REPORT.—Each registered proxy advi-
11 sory firm shall, at the beginning of each fiscal year of such
12 firm, report to the Commission on the number of share-
13 holder proposals its staff reviewed in the prior fiscal year,
14 the number of recommendations made in the prior fiscal
15 year, the number of staff who reviewed and made rec-
16 ommendations on such proposals in the prior fiscal year,
17 and the number of recommendations made in the prior
18 fiscal year where the proponent of such recommendation
19 was a client of or received services from the proxy advisory
20 firm.

21 “(l) TRANSPARENT POLICIES.—Each registered
22 proxy advisory firm shall file with the Commission and
23 make publicly available its methodology for the formula-
24 tion of proxy voting policies and voting recommendations.

25 “(m) RULES OF CONSTRUCTION.—

1 “(1) NO WAIVER OF RIGHTS, PRIVILEGES, OR
2 DEFENSES.—Registration under and compliance
3 with this section does not constitute a waiver of, or
4 otherwise diminish, any right, privilege, or defense
5 that a registered proxy advisory firm may otherwise
6 have under any provision of State or Federal law,
7 including any rule, regulation, or order thereunder.

8 “(2) NO PRIVATE RIGHT OF ACTION.—Nothing
9 in this section may be construed as creating any pri-
10 vate right of action, and no report filed by a reg-
11 istered proxy advisory firm in accordance with this
12 section or section 17 shall create a private right of
13 action under section 18 or any other provision of
14 law. Provided, however, that a subject of a proxy ad-
15 visory firm voting recommendations aggrieved by a
16 proxy advisory firm’s failure to comply in full with
17 subsection (g), or rules issued by the Commission
18 thereunder, may bring an action in Federal district
19 court to enforce said provisions through equitable re-
20 lief, money damages, or such other relief determined
21 by the court to be appropriate.

22 “(n) REGULATIONS.—

23 “(1) NEW PROVISIONS.—Such rules and regula-
24 tions as are required by this section or are otherwise

1 necessary to carry out this section, including the ap-
2 plication form required under subsection (a)—

3 “(A) shall be issued by the Commission,
4 not later than 180 days after the date of enact-
5 ment of this section; and

6 “(B) shall become effective not later than
7 1 year after the date of enactment of this sec-
8 tion.

9 “(2) REVIEW OF EXISTING REGULATIONS.—Not
10 later than 270 days after the date of enactment of
11 this section, the Commission shall—

12 “(A) review its existing rules and regula-
13 tions which affect the operations of proxy advi-
14 sory firms;

15 “(B) amend or revise such rules and regula-
16 tions in accordance with the purposes of this
17 section, and issue such guidance, as the Com-
18 mission may prescribe as necessary or appro-
19 priate in the public interest or for the protec-
20 tion of investors; and

21 “(C) direct Commission staff to withdraw
22 the Egan Jones Proxy Services (May 27, 2004)
23 and Institutional Shareholder Services, Inc.
24 (September 15, 2004) no-action letters.

1 “(o) APPLICABILITY.—This section, other than sub-
2 section (n), which shall apply on the date of enactment
3 of this section, shall apply on the earlier of—

4 “(1) the date on which regulations are issued in
5 final form under subsection (n)(1); or

6 “(2) 270 days after the date of enactment of
7 this section.”.

8 (b) CONFORMING AMENDMENT.—Section 17(a)(1) of
9 the Securities Exchange Act of 1934 (15 U.S.C.
10 78q(a)(1)) is amended by inserting “proxy advisory firm,”
11 after “nationally recognized statistical rating organiza-
12 tion,”.

13 **SEC. 4. COMMISSION ANNUAL REPORT.**

14 The Commission shall make an annual report publicly
15 available on the Commission’s Internet website. Such re-
16 port shall, with respect to the year to which the report
17 relates—

18 (1) identify applicants for registration under
19 section 15H of the Securities Exchange Act of 1934,
20 as added by this Act;

21 (2) specify the number of and actions taken on
22 such applications;

23 (3) specify the views of the Commission on the
24 state of competition, transparency, policies and

1 methodologies, and conflicts of interest among proxy
2 advisory firms;

3 (4) include the determination of the Commis-
4 sion with regards to—

5 (A) the quality of proxy advisory services
6 issued by proxy advisory firms;

7 (B) the financial markets;

8 (C) competition among proxy advisory
9 firms;

10 (D) the incidence of undisclosed conflicts
11 of interest by proxy advisory firms;

12 (E) the process for registering as a proxy
13 advisory firm; and

14 (F) such other matters relevant to the im-
15 plementation of this Act and the amendments
16 made by this Act, as the Commission deter-
17 mines necessary to bring to the attention of the
18 Congress;

19 (5) identify problems, if any, that have resulted
20 from the implementation of this Act and the amend-
21 ments made by this Act; and

22 (6) recommend solutions, including any legisla-
23 tive or regulatory solutions, to any problems identi-
24 fied under paragraphs (4) and (5).

○