AUTHENTICATED
U.S. GOVERNMENT
INFORMATION
GPO

REFORMING THE PROXY PROCESS TO SAFEGUARD INVESTOR INTERESTS

HEARING

BEFORE THE

SUBCOMMITTEE ON CAPITAL MARKETS

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED EIGHTEENTH CONGRESS

FIRST SESSION

JULY 13, 2023

Printed for the use of the Committee on Financial Services

Serial No. 118–38

U.S. GOVERNMENT PUBLISHING OFFICE
53–377 PDF WASHINGTON : 2024

HOUSE COMMITTEE ON FINANCIAL SERVICES

PATRICK MCHENRY, North Carolina, *Chairman*

FRANK D. LUCAS, Oklahoma
PETE SESSIONS, Texas
BILL POSEY, Florida
BLAINE LUETKEMEYER, Missouri
BILL HUIZENGA, Michigan
ANN WAGNER, Missouri
ANDY BARR, Kentucky
ROGER WILLIAMS, Texas
FRENCH HILL, Arkansas, *Vice Chairman*
TOM EMMER, Minnesota
BARRY LOUDERMILK, Georgia
ALEXANDER X. MOONEY, West Virginia
WARREN DAVIDSON, Ohio
JOHN ROSE, Tennessee
BRYAN STEIL, Wisconsin
WILLIAM TIMMONS, South Carolina
RALPH NORMAN, South Carolina
DAN MEUSER, Pennsylvania
SCOTT FITZGERALD, Wisconsin
ANDREW GARBARINO, New York
YOUNG KIM, California
BYRON DONALDS, Florida
MIKE FLOOD, Nebraska
MIKE LAWLER, New York
ZACH NUNN, Iowa
MONICA DE LA CRUZ, Texas
ERIN HOUCHIN, Indiana
ANDY OGLES, Tennessee

MAXINE WATERS, California, *Ranking Member*
NYDIA M. VELÁZQUEZ, New York
BRAD SHERMAN, California
GREGORY W. MEEKS, New York
DAVID SCOTT, Georgia
STEPHEN F. LYNCH, Massachusetts
AL GREEN, Texas
EMANUEL CLEAVER, Missouri
JIM A. HIMES, Connecticut
BILL FOSTER, Illinois
JOYCE BEATTY, Ohio
JUAN VARGAS, California
JOSH GOTTHEIMER, New Jersey
VICENTE GONZALEZ, Texas
SEAN CASTEN, Illinois
AYANNA PRESSLEY, Massachusetts
STEVEN HORSFORD, Nevada
RASHIDA TLAIB, Michigan
RITCHIE TORRES, New York
SYLVIA GARCIA, Texas
NIKEMA WILLIAMS, Georgia
WILEY NICKEL, North Carolina
BRITTANY PETTERSEN, Colorado

MATT HOFFMANN, *Staff Director*

SUBCOMMITTEE ON CAPITAL MARKETS

ANN WAGNER, Missouri, *Chairwoman*

FRANK D. LUCAS, Oklahoma
PETE SESSIONS, Texas
BILL HUIZENGA, Michigan
FRENCH HILL, Arkansas
TOM EMMER, Minnesota
ALEXANDER X. MOONEY, West Virginia
BRYAN STEIL, Wisconsin
DAN MEUSER, Pennsylvania
ANDREW GARBARINO, New York, *Vice Chairman*
MIKE LAWLER, New York
ZACH NUNN, Iowa
ERIN HOUCHIN, Indiana

BRAD SHERMAN, California, *Ranking Member*
GREGORY W. MEEKS, New York
DAVID SCOTT, Georgia
JUAN VARGAS, California
JOSH GOTTHEIMER, New Jersey
VICENTE GONZALEZ, Texas
SEAN CASTEN, Illinois
WILEY NICKEL, North Carolina
STEPHEN F. LYNCH, Massachusetts
EMANUEL CLEAVER, Missouri

CONTENTS

Page

Hearing held on:
July 13, 2023 1
Appendix:
July 13, 2023 41

WITNESSES

THURSDAY, JULY 13, 2023

Berry, Jonathan, Managing Partner, Boyden Gray PLLC 5
Doyle, Tim, Senior Policy Advisor, Bipartisan Policy Center (BPC) 7
Minow, Nell, Vice Chair, ValueEdge Advisors 12
Netram, Chris, Managing Vice President, Policy, National Association of Manufacturers (NAM) 8
White, Joshua T., Assistant Professor of Finance and the Brownlee O. Currey Jr. Dean's Faculty Fellow, Vanderbilt University's Owen Graduate School of Management 10

APPENDIX

Prepared statements:
Berry, Jonathan 42
Doyle, Tim 67
Minow, Nell 80
Netram, Chris 99
White, Joshua T. 114

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

Lucas, Hon. Frank D.:
Additional information provided in response to questions posed during the hearing to Tim Doyle 126
Meuser, Hon. Dan:
Written responses to questions for the record submitted to Jonathan Berry 128
Waters, Hon. Maxine:
Better Markets Fact Sheet, "ESG Investing is Here to Stay" 214
Written statement of Green America 223
Written statement of the Interfaith Center on Corporate Responsibility ... 229
Written statement of Out Leadership 231
Written statement of Principles for Responsible Investment 237
Written statement of the Shareholder Rights Group 244
Written statement of various farmers and ranchers groups 250
Written statement of various investor organizations 256
Written statement of various undersigned organizations 259
Written responses to questions for the record submitted to Jonathan Berry 265
Written responses to questions for the record submitted to Tim Doyle 266
Written responses to questions for the record submitted to Nell Minow 267
Written responses to questions for the record submitted to Chris Netram . 268
Written responses to questions for the record submitted to Joshua T. White 269

REFORMING THE PROXY PROCESS TO SAFEGUARD INVESTOR INTERESTS

Thursday, July 13, 2023

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON CAPITAL MARKETS,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:05 a.m., in room 2128, Rayburn House Office Building, Hon. Ann Wagner [chairwoman of the subcommittee] presiding.

Members present: Representatives Wagner, Lucas, Huizenga, Hill, Steil, Meuser, Garbarino, Lawler, Nunn, Houchin; Sherman, Meeks, Scott, Vargas, Gottheimer, Gonzalez, Casten, Nickel, Lynch, and Cleaver.

Ex officio present: Representative Waters.

Chairwoman WAGNER. Good morning. The Subcommittee on Capital Markets will come to order.

Without objection, the Chair is authorized to declare a recess of the subcommittee at any time.

Today's hearing is entitled, "Reforming the Proxy Process to Safeguard Investor Interests."

I want to ask for a point of personal privilege from the ranking member to recognize one of our staff, one of the minority staff members, if that is okay with you, sir?

Mr. SHERMAN. It would be objectionable to me if we didn't.

[laughter]

Chairwoman WAGNER. I do want to take this point of personal privilege and recognize one of our really important staffers, whose last day with the committee will be tomorrow, after about 4½ years. Bring him out here. Don't let him hide back there. Is he here? Okay, good. I want to recognize Franklin Thornton. Franklin, stand up.

[applause]

Franklin served the committee as a committee clerk in the 117th Congress, and was extremely helpful and patient to our Members on both sides of the aisle during much of our COVID-19 pandemic when hearings, and markups, and doing everything online via Webex was very difficult. So, I want to thank him for facilitating those hearings and those markups, and I want to thank him for his service, and I think we all wish him the best on his next career in Denver. So Franklin, thank you for everything.

[applause]

Chairwoman WAGNER. And now we will move on, and I will recognize myself for 4 minutes to give an opening statement.

Thank you all for joining us today. This hearing will examine policies that prioritize increased transparency, accountability, and economic analysis in shareholder voting decisions, while also addressing concerns with the outsized influence of proxy advisor firms.

I am greatly concerned with the Biden Administration's continued efforts to force non-material environmental, social, and political issues on American companies and investors. Prioritizing these ideologically-driven regulations drives up the costs and burdens of participating in the U.S. public markets. This, in turn, diminishes the appeal for private companies considering going public or remaining a public company, and fewer publicly-traded companies means fewer investment opportunities for Main Street investors. These increased costs hinder the ability of American public companies to compete on a global scale, putting them at a disadvantage, while China's economic influence continues to grow. What is even more concerning is that these policies end up burdening retail investors, who rely on solid financial returns to save for retirement, purchase a home, or pay for their child's education.

We must remember that the primary purpose of our public markets is to foster economic growth. Unfortunately, unrestricted shareholder activism is diverting attention and limited resources from core issues undermining the attractiveness of U.S. markets and discouraging companies from going public. The prioritization of shareholder proposals that deviate from a company's strategic direction or long-term goals has transformed boardrooms into partisan platforms where fringe political agendas overshadow sound financial management and business strategy.

For our public markets to remain focused on long-term shareholder value, it is crucial to reform the proxy process to reduce the financial burdens on small and mid-sized companies and minimize distractions for management. By ensuring that shareholders' proposals align with a company's interests and long-term goals, we will promote value creation for all shareholders.

Today, we will also discuss the Biden Administration's imposition of climate reporting and other requirements that place unnecessary burdens on companies, hindering their ability to grow and compete in a global economy. For example, the SEC's proposed 500-page climate disclosure rule would replace voluntary sustainability reports with mandatory disclosures, including detailed emissions data and climate risk management strategies. Congress has not granted the SEC the authority to create regulations that compel companies to disclose general information about environmental, social, and governance (ESG) issues. In fact, Congress repeatedly expressed dissatisfaction with the current number and complexity of disclosures the SEC requires and repeatedly urged the agency to simplify them rather than adding to their complexity.

Piling on pages of complicated disclosures minimizes their usefulness to Main Street investors and impedes the ability of younger, smaller companies to compete against large incumbents. In light of these challenges, it is crucial that we address these issues with a focus on fostering economic growth, promoting sound financial regulations, and reducing unnecessary burdens on American businesses.

I very much look forward to hearing from our esteemed panel of experts today as we delve deeper into these matters in order to safeguard the interests of Main Street investors.

The Chair now recognizes the ranking member of the subcommittee, the gentleman from California, Mr. Sherman, for 4 minutes for an opening statement.

Mr. SHERMAN. And I would ask unanimous consent that if the ranking member of the full Financial Services Committee isn't here to give her 1-minute opening statement, that she can do it after one or all of the witnesses.

Chairwoman WAGNER. Without objection, it is so ordered.

Mr. SHERMAN. This month, we have a series of hearings designed to prevent shareholders from getting the information they want to decide whether to invest and make sure that those shareholders don't affect the behavior of the corporations they own. We prevent investors from making decisions based on any criteria not approved by the Governors of Florida and Texas by depriving them of information, and then, in this morning's hearing, preventing them from introducing resolutions, and in this afternoon's hearing, preventing them from getting the advice they need to decide how to vote on those resolutions.

We are told that these considerations are fringe or immaterial, and there are those who say that it is material only if it is 5 percent of earnings per share, but the Republican witness correctly testified yesterday that what is material, is what is important to investors. Now, there may be a few unusual investors. Yesterday, I posited the idea of someone who only wants to invest in companies whose boardrooms are painted purple. Those folks do not need to be catered to, but where a material portion of the investment community finds something material, it is our job to get them the information and to allow them to affect the corporate behavior of the companies they own.

There are at least two groups of investors, the first I call the, "Ebenezer Scrooge investors," who are interested only in earnings per share, but even they need information about global warming. They have to decide whether to invest in the Maldives Coconut Plantation Corporation, and they will get an SEC document that details the risk factors in terms of competition. Coconuts might be grown elsewhere, but if you are going to invest in the Maldives Plantation Corporation, you also need information about another risk factor, inundation, because the Maldives are only 4 feet above sea level. Even the, "Ebenezer Scrooge invester," needs information about the effect of global warming on earnings per share.

Second, we have the, "John Denver investors." This is hundreds of billions of dollars of investment capital that cares what the effect of their investment is on our environment, and if we don't provide them with the information they want, many of them will invest in European companies that do provide that information.

And third, what I call the, "John Bolton investors," those who are concerned about the national security impacts of the investments they make.

Today, we are going to focus on the rules for introducing a resolution, and we have the Republican SEC raise that. You have to be an investor of $25,000 worth of shares for a period of 1 year.

I might go along with that, but what I can't go along with is they prevent aggregation. What would this mean in the context of running a political campaign? What if we said that any contribution of under $2,000 cannot be accepted by a campaign? So, if you can run your campaign with only $2,000 and up, fine, but if you have 100 donors who want to give you $20, that doesn't count. Shareholders who invest $1,000 or $500 in a corporation, if there are a lot of them, should count just as much as one investor with $25,000 of investment.

We are told that the SEC should, in effect, conspire, collude with corporate boards to keep out of the proxy statement resolutions on certain topics, and look at how these topics overlap. One topic is that you shouldn't have something that doesn't relate to the company's business and at least 5 percent of the business. The other says you shouldn't have a resolution that relates to ordinary business operations. So if it doesn't relate to the company's business, you can't propose it, and if it does relate to the company's business, you can't propose it. Thank God today's SEC is no longer issuing no-action letters that, in effect, disempower all shareholders.

We are told that this is about cost. It isn't. This hearing is being held for those who think these resolutions might win, and they don't want to give these shareholders a chance.

I yield back.

Chairwoman WAGNER. The gentleman's time has expired. The Chair now recognizes the gentleman from Michigan, Mr. Huizenga, who is also the Chair of our Subcommittee on Oversight and Investigations, for 1 minute for an opening statement.

Mr. HUIZENGA. Thank you, Madam Chairwoman. I appreciate you having this hearing today. Last year, ESG shareholder proposals continued their upward trajectory as activist investors continued their assault on the returns of actual retail investors. At the center of this debate are the proxy advisory firms, which in many cases support policies that run counter to their own fiduciary responsibility to maximize returns for investors. Coupled with the recent politicization of the SEC, proxy advisory firms have seized immense power to shift policy, often using a one-size-fits-all framework to promote a liberal social and political agenda. The proxy process is broken. It no longer promotes long-term shareholder value and operates without transparency or accountability and ignores materiality.

As the Biden Administration continues to focus on implementing costly environmental, social, and political-based regulatory requirements, which have significant ramifications for U.S. public markets, Republicans will promote policies that protect retail investors, maximize returns, and increase financial security. I yield back.

Chairwoman WAGNER. The gentleman yields back. The Chair now recognizes the ranking member of the Full Committee, the gentlelady from California, Ms. Waters, for 1 minute.

Ms. WATERS. Thank you very much, Madam Chairwoman. I would like to take a point of personal privilege to acknowledge Franklin Thornton, who served our committee as clerk for the past 2 years, including during the difficult months during the pandemic. His patience and professionalism enabled the committee to conduct its business during that time. And for the past few months, he has

been serving dutifully on our housing policy team, and I would like to wish him the best in his future endeavors.

Chairwoman WAGNER. Thank you. We did the same at the opening. We are all so grateful for Franklin, and we wish him the best as he moves on. Thank you.

Ms. WATERS. Thank you very much. Today, Republicans are giving the term, "investor protection," new meaning by pushing legislation that would protect investors from their own ideas. For a party that supposedly values free speech and free market capitalism, they are now trying to muzzle the ability of shareholders to bring forth proposals that can influence the direction of the companies they own. MAGA Republicans would prefer that shareholders only be able to vote on what corporate management wants, completely avoiding any sense of accountability or transparency. When it comes to corporate board decision-making, this committee has real work to do when it comes to investor protection, and this paternalistic, disingenuous approach to shareholder rights is not it. I yield back.

Chairwoman WAGNER. The gentlelady yields back.

We now welcome the testimony of our witnesses: Mr. Jonathan Berry, managing partner of Boyden Gray PLLC; Mr. Tim Doyle, a senior policy advisor at the Bipartisan Policy Center and the founder of Doyle Strategies LLC; Mr. Chris Netram, the managing vice president of policy at the National Association of Manufacturers; Dr. Joshua White, an assistant professor of finance and the Brownlee O. Currey Jr. Dean's Faculty Fellow at Vanderbilt University's Owen Graduate School of Management; and Ms. Nell Minow, the vice chair of ValueEdge Advisors. We thank you all for your testimony here today, and we will now get started.

Mr. Berry, you are now recognized for 5 minutes to give your oral remarks.

STATEMENT OF JONATHAN BERRY, MANAGING PARTNER, BOYDEN GRAY PLLC

Mr. BERRY. Thank you. Good morning, Chairwoman Wagner, Ranking Member Sherman, and members of the subcommittee. My name is Jonathan Berry, and I am the managing partner of the law and policy strategy firm, Boyden Gray. I was previously the Acting Assistant Secretary for Policy at the U.S. Department of Labor during the Trump Administration. I also currently represent the National Center for Public Policy Research and other shareholder clients in litigation against the SEC regarding its shareholder proposal rule, 14a-8. While my views on the subject of today's hearing are informed by that work, I do not appear here today on behalf of any client, and the views I present are my own.

Politically-motivated shareholder proposals are a main entry point by which ESG-focused activists, and money managers, and advisors influence public companies to adopt their agendas. This process starts with 14a-8. Now, the SEC did not invent the shareholder proposal. To the contrary, prior to 14a-8, there existed and still exists a robust system of State corporate law governing proposals. While Exchange Act Section 14-a gave the Commission authority to compel disclosures of existing information, Congress left the substantive regulation of stockholder meetings to State law, as

was traditional. Rule 14a-8 upended this arrangement, first by compelling companies to include shareholder proposals and, over time, by contorting the law governing the substance of shareholder proposals in ways far beyond State law.

For a time, the SEC permitted the exclusion of social proposals if they also related to the company's ordinary business operations, but in 1998, the Commission narrowed the ordinary business exclusion to prevent excluding proposals that, "focus on sufficiently-significant social policy issues." The SEC opened the gates even wider in 2021 with a staff bulletin effectively cutting ties between social proposals and ordinary business completely. Environmental and social proposals now represent a majority of all proposals in Russell 3000 companies, and 58 percent of proposals in 2022.

While so-called anti-ESG proposals have risen somewhat, the SEC has blocked many of them from consideration on company proxy statements. This last proxy season, my client, the National Center for Public Policy Research, took a shareholder proposal that the SEC had blessed on a discrimination issue and substituted the terms, "viewpoint" and "ideology," for the prior proposal's terms, "sexual orientation" and "gender identity." But the SEC said that my client's proposal could be struck off the ballot, that viewpoint discrimination in the workplace was not a significant social policy question.

The SEC's pattern of disfavoring conservative proposals is the only rational explanation for the disparity here, and we see the pattern. A recent analysis found that the SEC granted no-action relief on 46 percent of all requests for liberal-aligned proposals but 72 percent of all conservative-aligned ones. Put the SEC's viewpoint filter on top of the enormous volume of pro-ESG proposals that activists put out, and you see why pro-ESG viewpoints are overrepresented in the proxy process.

Now, once proposals make it to the shareholder ballot, the rest of the proxy process takes over to use the proposal as an opportunity to pressure companies to adopt ESG goals. Here, I want to call attention to the proxy advisory firms in particular. ISS and Glass Lewis control upward of 90 percent of the relevant market, and, for example, ISS recommends voting against directors of many companies flagged by climate activists unless the company has issued detailed disclosures of its climate-related risks and implemented net-zero-by-2050 reduction targets. Both advisors threaten in their voting guidelines directors at companies that fail to respond to proposals that receive broad shareholder support, and Glass Lewis guidelines seem to say that even 20 percent counts as broad support.

I would like to close by applauding the committee for grasping the fundamental nature of the problems caused by Rule 14a-8 and supporting the exclusion of shareholder proposals if the subject matter is environmental, social or political, and ultimately barring 14a-8 altogether. I commend the committee's focus on ensuring proxy advisors and asset managers face greater accountability for how they recommend and vote on shareholder proposals, and I would also like to note there is increasing activity in the States on these subjects.

I thank the committee again.

[The prepared statement of Mr. Berry can be found on page 42 of the appendix.]

Chairwoman WAGNER. Thank you, Mr. Berry.

Mr. Doyle, you are now recognized for 5 minutes to give your oral remarks.

STATEMENT OF TIM DOYLE, SENIOR POLICY ADVISOR, BIPARTISAN POLICY CENTER (BPC)

Mr. DOYLE. Good morning, Chairwoman Wagner, Ranking Member Sherman, Ranking Member Waters, and members of the subcommittee. Thank you for inviting me to testify today. My name is Tim Doyle, and I am the senior policy advisor at the Bipartisan Policy Center, or BPC, where I provide subject matter expertise on corporate governance and ESG-related matters.

BPC is a nonprofit organization founded in 2007 by four former Senate Majority Leaders: Howard Baker, Tom Daschle, Bob Dole, and George Mitchell. BPC drives principled and politically-viable policy solutions through analysis and negotiation, and by providing a forum for diverse views. BPC's funding reflects the character and diversity of the organization in that it comes from charitable philanthropies, individuals, and corporate donors. As such, we believe all donors have unique and diverse interests. However, we believe that bipartisanship is the only way to forge a sustainable public policy solution. It is with that policy philosophy that I testify today.

BPC has been evaluating and discussing ESG-related issues for a number of years now. We have learned that the key to understanding ESG is looking into how one intends to use the ESG data. As a result, the use of the ESG acronym varies widely depending on sector, company, and an individual's perspective. Given the difficulty in fully understanding the breadth of ESG-related topics, the committee should continue to work collaboratively with nonprofits, think tanks, academics, and, of course, investors and issuers in finding common language when using the term, "ESG."

The ESG debate raises profound questions about the way to deliver returns for investors. The next few years will determine what comprises ESG in the future or even whether the term has lasting power. Furthermore, given the exponential growth in ESG investment funds and other financially-based uses of the term, "ESG," establishing some consensus around the definition of, "ESG," would greatly improve the capital markets, further protect retail investors, and ultimately encourage more companies to go public.

Of course, at the center of the ESG debate is disclosure. Determining what is disclosed involves numerous factors depending on if it is legislatively mandated, regulatorily required, or individually requested at annual shareholder meetings. My written testimony focuses on the regulatory requirement disclosure, which, historically, is used in materiality analysis, and also for or regarding the need for enhanced oversight of the proxy advisors, given the influence that their voting recommendations have on ESG-related issues.

Materiality has been a standard used for determining disclosure at least since the 1976 Supreme Court case, *TSC Industries, Inc.* v. *Northway, Inc.* What many don't realize is that leading up to the holding in that case was years of litigation involving disclosure.

The, "reasonable investor," standard described in that case was itself a compromise in that it provided analysis to be used so investors would receive enough information to make informed investment decisions, but not so much as to become overwhelmed with an avalanche of data, as the Court stated. This standard has stood the test of time, and this committee should strongly consider codifying that decision if, for no other reason than to bring some regulatory certainty and disclosure for both investors and issuers.

The growth of the proxy advisory industry is, in some ways, an example of a success story. The transition from defined benefit to defined contribution retirement plans resulted in the exponential growth of institutional investors over the last couple of decades. This, in turn, has created the potential need to vote on thousands of shareholder proposals. It is all too clear, however, that proxy advisors began to have what some have called an oversized influence on the proxy process, and ultimately, an indirect, and in some cases, a direct influence over corporate disclosure and policy.

We sometimes forget that the proxy advisors are for-profit entities, and inherent in that is a conflict between their recommendations and their clients. Moreover one proxy firm, in particular, even started providing consulting services to the same companies for which they were providing recommendations. In both scenarios, the appearance of impropriety requires enhanced transparency and accountability to protect investors and ensure a strong capital market.

Another issue that is regularly raised is that some proxy advisor reports which are used to make recommendations have errors in them that may well affect voting results on certain proposals. This committee should develop policies that ensure transparency to alleviate the conflicts of interest, to protect investors, and to create a framework for issuers to correct errors before proposals are voted on. It is important to mention that many of these issues have had bipartisan support. For example, proxy reform, which has been contemplated by the SEC for more than a decade, has previously had congressional support. There have also been several Republican- and Democratic-appointed Commissioners at the SEC who have supported reforming the proxy process, including additional oversight of proxy advisory firms.

In closing, I truly appreciate the opportunity to share some of what we have learned over the last few years at BPC. Thank you very much.

[The prepared statement of Mr. Doyle can be found on page 67 of the appendix.]

Chairwoman WAGNER. Thank you, Mr. Doyle.

Mr. Netram, you are now recognized for 5 minutes to give your oral remarks.

STATEMENT OF CHRIS NETRAM, MANAGING VICE PRESIDENT, POLICY, NATIONAL ASSOCIATION OF MANUFACTURERS (NAM)

Mr. NETRAM. Good morning, Chairwoman Wagner, Ranking Member Sherman, Ranking Member Waters, and members of the subcommittee. My name is Chris Netram, and I am the managing vice president of policy at the National Association of Manufacturers (NAM). I appreciate the opportunity to testify today on behalf

of the NAM's 14,000 members and the 13 million men and women who make things in America.

Manufacturing supports local communities across the country, creating well-paying jobs for Americans from all walks of life. Manufacturing pioneers groundbreaking technologies and lifesaving innovations, and manufacturing is an economic driver that powers growth here at home and supports American competitiveness on the world stage. Manufacturing is capital-intensive, and manufacturers often turn to the public markets to finance investments that create jobs and strengthen communities. The public market allows businesses to access capital, and it lets Americans share in the industry's success. Investments like mutual funds and pension plans help workers save for a child's education, a new home, or a secure retirement.

Manufacturers have a fiduciary duty to act in these Main Street investors' financial best interest. Focusing on financial returns helps businesses grow and safeguards investors' retirement security, but in recent years, third parties have hijacked the proxy process to distract companies from this duty. Activists use the proxy ballot to advance political and social agendas, proxy firms dictate corporate governance decisions, and the SEC is empowering these groups while also proposing ESG disclosure mandates of its own.

As you have already heard, ESG proposals are at an all-time high. They now make up approximately 60 percent of all proposals, and it takes only $2,000 to get an ID on a ballot. The SEC is encouraging these proposals, telling companies that anything with broad societal impact can't be excluded from the proxy ballot, even if totally unrelated to a business's operations. Turning the proxy ballot into a debate club diverts time and resources away from shareholder value creation and forces companies to wade into controversial topics over which they have no control. Congress must prevent the SEC from empowering activists and forcing companies to include irrelevant proposals on their ballots.

Cheerleading for activists are proxy advisory firms, where proxy firms' influence goes well beyond ESG proposals. Their policies shape corporate decisions, and their recommendations dictate shareholder votes. Despite their power, proxy firms operate with minimal regulatory oversight, and the SEC has, in fact, rescinded the modest protections that were adopted in 2020 to inform and protect investors. This means that the firm's conflicts of interest, errors, and lack of transparency go largely unchecked. Nevertheless, asset managers continue to rely on their services, in many instances even allowing proxy firms to robo-vote on their behalf. In other words, unaccountable, error-prone firms are robo-voting on decisions that affect Americans' retirement savings.

I want to take this opportunity to thank Congressman Steil for his years of leadership on legislation to rein in proxy firms. Manufacturers believe that Congress must act to require the firms to engage with businesses, protect investors from conflicts of interest, enforce anti-fraud standards, and limit robo-voting.

Not only is the SEC empowering proxy firms and ESG activists, the agency is also undertaking an ESG agenda of its own. New ESG disclosure mandates threaten to increase costs and liability for manufacturers and overwhelm investors with immaterial infor-

mation. Even small and privately-held businesses will feel these effects. That is because many of these new requirements impact supply chains, like the climate rule, Scope 3, mandate. Investors need material information to make informed investing decisions and grow their retirement savings. Instead, the SEC has proposed far-reaching mandates that won't inform investors but will harm manufacturers. Congress must limit the SEC's regulatory onslaught and require the agency to focus only on material disclosures.

In conclusion, manufacturers believe strongly in the importance of tackling climate change, improving sustainability, and enhancing diversity. Taking a company-specific approach to these issues can support business growth and drive shareholder returns, but politically-motivated activists are pursuing inflexible ESG agendas with little regard to their impact on everyday Americans' financial security, and the SEC is increasingly a partner in that effort. If this trend is allowed to continue, small manufacturers will be the hardest hit. I have spoken to small manufacturers around the country who are deeply concerned about potentially losing public company customers and are facing insurmountable regulatory costs because they just can't keep up with ESG.

Thank you for the opportunity to testify today, and I look forward to answering your questions.

[The prepared statement of Mr. Netram can be found on page 99 of the appendix.]

Chairwoman WAGNER. Thank you, Mr. Netram.

Dr. White, you are now recognized for 5 minutes for your oral remarks.

STATEMENT OF JOSHUA T. WHITE, ASSISTANT PROFESSOR OF FINANCE AND THE BROWNLEE O. CURREY JR. DEAN'S FACULTY FELLOW, VANDERBILT UNIVERSITY'S OWEN GRADUATE SCHOOL OF MANAGEMENT

Mr. WHITE. Thank you, Chairwoman Wagner, Ranking Member Sherman, Ranking Member Waters, and members of the Subcommittee on Capital Markets. Thank you for inviting me today to discuss reforms of the proxy process. I look forward to your questions on this important issue.

The House Financial Services Committee is considering several legislative proposals aimed at safeguarding investor interests. These issues are paramount for ordinary investors who put their money into public equities to save for college or retirement. In my written testimony, I discuss what I believe are three key challenges running counter to the interests of most investors. The first is a dramatic upswing in the volume of non-governance ESG shareholder proposals. The second is the influence of proxy advisory firms on managers' and institutional investor behavior. And the third is costly SEC mandates to disclose non-material public information that reduces the attractiveness of U.S. capital markets. I ask that my written testimony be entered into the record.

The proxy voting process plays a pivotal role in corporate governance. It is how most shareholders vote for directors who have a fiduciary duty to represent their interests. Equity investors also vote on other matters, such as advisory votes on any shareholder proposals that appear on the proxy. In the past 2 years, we have seen

a record number of environmental and social proposals, which are the, "E'," and "S," component of ESG, with the, "G," representing governance. Managers can ask the SEC to exclude shareholder proposals from the proxy, which is known as no-action relief. Research shows that the stock price tends to increase when the SEC approves such exclusions. This suggests that managers are skilled at spotting proposals that risk investor welfare and only serve to advance special interests.

In November 2021, the SEC updated its exclusion policy with Staff Legal Bulletin 14L, which notes the SEC will no longer honor prior admission policies if a proposal has significant social policy implications. In my written testimony, I provide data analysis showing the profound influence that this bulletin had on proxy voting. In 2022, there was a 100-percent surge in environmental and social proposals, yet investor support for these proposals plummeted. In July of 2022, the SEC proposed additional changes to the rule underlying proposal exclusions. If adopted, it will make it even more challenging for managers to omit proposals they perceive as harmful to shareholder value. The cost of shareholder proposals is substantial and includes both the legal costs and, more importantly, the time that managers and directors spend addressing proposals.

Flooding the proxy with environmental and social proposals likely overwhelms investors, potentially leading to less-informed voting on critical issues. Institutional investors often rely on proxy advisory firms, which provide fee-based voting recommendations to its clients. Their reports can help passive portfolio managers reduce the cost of voting on thousands of proxies. However, there are concerns about the power of proxy advisors in the U.S. as there are only two firms that dominate the market. Studies show that their voting and advice is highly influential, but concerns arise with this influence.

Some show that certain institutional advantage investors managing trillions of dollars follow their advice more than 95 percent of the time. This is known as robo-voting, which poses multiple issues. Research indicates that asset managers who rely less on proxy advice yield higher returns for their investors. That implies that robo-voting can negatively impact the majority of investors. One study finds that the largest proxy advisor often skews its environmental and social recommendations due to pressure from sponsors of those proposals, who know that those proxy advisors will bring in robo-voting. Managers and directors might also proactively adopt environmental and social proposals that destroy value to avoid negative attention or negative recommendations from proxy advisors on their own board seats.

Finally, I am concerned about some of the SEC's recent rulemakings. These endeavors mandate the disclosure of non-material information. Shifting away from the materiality standard for disclosure can harm investors and can harm the company by revealing proprietary disclosure costs. When the benefits do not outweigh the costs of disclosure, it should not be mandated.

Together, these three forces place pressure on public companies and discourage private companies from going public. The end result is lower return for shareholders, and fewer investment or diver-

sification opportunities for retail investors who lack access to investing in public companies. Thank you.

[The prepared statement of Dr. White can be found on page 114 of the appendix.]

Chairwoman WAGNER. Thank you, Dr. White.

And Ms. Minow, you are now recognized for 5 minutes for your oral remarks.

STATEMENT OF NELL MINOW, VICE CHAIR, VALUEEDGE ADVISORS

Ms. MINOW. Thank you very much, Madam Chairwoman, and members of the subcommittee, for this opportunity to speak to you. I want to associate myself with the opening remarks made by Ranking Members Sherman and Waters and thank them very much for the roundtable they presided over yesterday, and I recommend that everyone on the committee and the staff take a look at that.

Many years ago, I was talking to a corporate director who was very unhappy with the vote on a shareholder proposal, and he said, "You have to understand now those are fringe shareholders." And I said, "The vote got a 60 percent vote in favor, which means you are the fringe."

We have talked a little bit about what is material, and I will tell you, as Ranking Member Sherman said yesterday, the best people to decide what information is material are the investors. As much as I appreciate the opportunity to speak to you today, I particularly appreciate the opportunity to remind some of the members of this panel, including the National Association of Manufacturers, of how capitalism works.

"Capitalism" is named for the providers of capital. It is provided for the shareholders. And as I guess the only person on this panel who has actually filed a shareholder proposal, I can tell you that we have talked a lot about the costs, which I have to say are grossly overestimated by self-reported figures, but not about the benefits. I think it is of tremendous benefit. You would think that the National Association of Manufacturers would be talking about their recognition of the importance of sustainability if they hadn't heard from their shareholders. I don't think they would, so I have a few key points.

Only a small percentage of companies receive any shareholder proposals, the household name companies get a lot, and many companies get one or two, but the vast majority get none. The average is one every 7 years, so it is really not a huge problem. Even a 100-percent vote in favor of a shareholder proposal is not binding. Companies are free to ignore it. It is a wonderful way, a very cost-effective way on both sides for shareholders to raise issues of importance.

A lot of these resolutions have been characterized as political. Again, as with material, it is up to the investors to decide what is political and what is material. So if the vote is nonbinding, the cost is really very minimal. Limiting shareholder proposals is killing the messenger, one of the very few ways insulated insiders get honest feedback. Now, I have heard a lot of complaints that a small number of individuals are responsible for a large percentage of

shareholder proposals, and that is true, but the important figure is the level of support that those proposals get. For example, 20 percent of the proposals filed by John Chevedden and Ken Steiner received support of more than 50 percent of shareholders, including a 79-percent vote at Duke Energy on a proposal that would require a simple majority vote rather than a supermajority for certain matters, and a 98-percent vote at Carlyle and a 99-percent vote at American Airlines. Again, these are not fringe shareholders, and these are not fringe issues. These are issues of vital importance to a wide and diverse variety of investors, of individuals, of index funds, of pension funds, and of all kinds of different funds. I think that, again, is how capitalism works.

I also want to point out that shareholder proposals are a very modest way to raise concerns at a low cost to investors and issuers. If shareholder proposals are limited further, the result will be challenges that are far more expensive and disruptive for everybody. I do want to make, if I may, Madam Chairwoman, a small correction to one of your points, which is that if a company goes private, that makes it not available for investment. In fact, the people I work with, the large pension funds, are huge investors in private equity. And I welcome anyone in the National Association of Manufacturers to go private at a fair price and see how they like dealing with private equity owners. I guarantee you the first thing that will happen is they will cut all the salaries.

Proxy advisor services are the exemplars of the free market. Nobody has to use their services. There is competition. There is a new anti-ESG proxy advisor that no one has mentioned, run as a side hustle by Presidential candidate, Vivek Ramaswamy, already being used by one of the large pension funds, so if there are no barriers to entry, nobody has to buy it. And if 90 percent follow the recommendations—and that is because 90 percent of the recommendations are a vote for the board of directors, a vote for the auditors—when it comes to the other issues, the more controversial issues, in fact, they depart from proxy advisors quite often.

Thank you very much, and I will be happy to answer any questions.

[The prepared statement of Ms. Minow can be found on page 80 of the appendix.]

Chairwoman WAGNER. Thank you, Ms. Minow.

We will now turn to Member questions, and I recognize myself for 5 minutes for questioning.

Dr. White, for more than 80 years, shareholders' engagement has been focused on a company's strategic direction, or perhaps their long-term goals would be a better way of putting it, with an eye on maximizing revenue and increased returns for investors. Recently, there has been an increase in the number of shareholder proposals that have turned boardrooms into partisan battlegrounds fighting over social agendas instead of focusing on sound financial management and business strategy. Could you please provide insights into the recent trends of politically-motivated shareholder proposals, specifically how this shift has changed the focus of corporate boards away from investors and companies' strength and onto external agendas untethered from the organization's financial health?

Mr. WHITE. Thank you, Chairwoman Wagner, for that question. Yes, I would agree that there has been a politicization in the corporate boardroom. Companies now have to misallocate what are scarce resources that investors provide them in hopes of generating a return. And they are focused not necessarily on the, "G," component of ESG, but more on the environmental and social component. As Ms. Minow pointed out, oftentimes, there are shareholder proposals to remove managerial entrenchment mechanisms, such as a supermajority vote. I just want to remind everyone that is the, "G," component of ESG, which academic research has shown for more than 20 years is valuable.

The environmental and social concerns are that, if you have a shareholder, or a subset of shareholders, or a minority shareholder that wants to push a special interest, they may be willing to sacrifice investment returns if it forwards their mission objective. That does not benefit all investors. In fact, if businesses do not run their organizations in the most efficient way, their competition will, and we compete on a global basis. To the extent that we politicize the boardroom, these burdens are just going to be passed onto public companies, which may then actually go private. That is what the research shows.

Chairwoman WAGNER. Okay. Mr. Netram, in November 2021, the SEC issued new guidance that made it difficult for companies to exclude ESG shareholder proposals. Staff Legal Bulletin 14L states that the SEC will now focus on the social policy significance of issues raised by shareholder proposals, rather than an individual company's connection to a particular issue. How significant of a departure is this from the SEC's longstanding criteria that relied on a proposal having a connection to the company's ordinary business operations?

Mr. NETRAM. It is incredibly significant. As we pointed out, this is a huge shift in the approach to these topics. What we have actually seen in practice is that granted requests for no-action relief after this rulemaking have fallen by about half. And what that means is that companies are now forced to deal with issues that are well outside of their control instead of being able to focus on things that are material to their underlying business.

Chairwoman WAGNER. So, the impact is large on businesses, on the shareholders, and on the retail investors at the end of the day?

Mr. NETRAM. That is correct.

Chairwoman WAGNER. Mr. Netram, it has been observed in the past that proxy firms, ISS and Glass Lewis, have released voting recommendations based on inaccurate and flawed data. I got incredible numbers yesterday, somewhere around 42 percent of those saying that this information is completely flawed and inaccurate. Investors who rely on the firms' recommendations are at risk of making uninformed decisions, undermining the integrity of the market. In this context, can companies review a proxy for recommendations and provide feedback to ensure that shareholders can make well-informed decisions when voting?

Mr. NETRAM. Currently, no. No such process exists for companies to make sure that the data that runs into the vote recommendations are accurate.

Chairwoman WAGNER. Why is it crucial for businesses to have the opportunity to review and offer feedback on draft proxy firm recommendations?

Mr. NETRAM. Because what we are talking about are, effectively, governance decisions on the direction of the business on which Main Street investors are relying for their retirement security. If those decisions are based on incomplete, inaccurate, or misleading data, the end result cannot be good.

Chairwoman WAGNER. And upwards of 42 percent is a very large amount. Would requiring proxy advisor firms to disclose their methodologies, calculations, and sources of information lead to a more transparent and reliable advisory process?

Mr. NETRAM. Absolutely.

Chairwoman WAGNER. I thank you, and I will yield back my time. And I recognize the gentlewoman from California, Ms. Waters, who is the ranking member of our full Financial Services Committee.

Ms. WATERS. Thank you so much, Madam Chairwoman. First, I would like Ms. Minow to know that you answered many of my questions about the value of shareholder proposals, and I would like to just have you comment further. As I mentioned, for a party that is supposedly pro-free-market capitalism and pro-investor-freedom, I find it incredibly ironic that Republicans want to limit the ability of the capitalists, shareholders, who are the owners of the companies that power our economy, from proposing initiatives to be voted on at corporate meetings. A key tenet of the Republican Party is that the government shouldn't be able to tell you what you can and can't do, but in the instances of our capital markets, they are trying to do just that. Republicans want to stifle the ordinary investor and their fiduciaries' ability to have a voice in how their investments are managed. Do you have any additional thoughts on that? If so, I would like to hear them.

Ms. MINOW. I appreciate that very much. There have been a lot of improvements over the years in boards of directors. When I first came to work in this field, O.J. Simpson was on five boards, and he was on an audit committee of one of them, and boards have become much more engaged, and much more qualified. That is all because of shareholder initiatives. That is all because of shareholder proposals. It was not unusual in those early days for a person to serve on 10 boards. Now, the average is two or three boards, and board members are doing a vastly better job because of shareholder proposals' management entrenchment devices. I am not here to say anything good about CEO pay, except to say it could be worse and it would be worse without the oversight of shareholders.

Again, I just want to emphasize that shareholder proposals are nonbinding. Companies can and do ignore the results of a shareholder proposal, and if that means the Chair would vote against the board next year, well, that is how the market responds. But yes, shareholder proposals have been enormously important, and I mentioned that 20 of John Chevedden's proposals got majority votes. I should also mention another 20 of them were successfully negotiated with the company in a manner that was satisfying to both sides.

Ms. WATERS. Thank you, Ms. Minow. Could you please discuss more how pension funds that the whole public shares engage the companies they own and their ability to engage companies in which they are invested through private funds? As I understand it, private funds don't make disclosures, neither of their investing practices or policies, nor do they make available information about the underlying portfolio companies. How are pension funds that are large investors and private funds, such as private equity funds or venture to capital funds, know whether the value of their investment is fair? How can they engage these private companies if they don't know about the governance or diversity metrics of these companies?

Ms. MINOW. Yes. Thank you, Ranking Member Waters. That is what, "private," means. And it has been my experience in working with large institutional investors that they are in very close touch with the managers and partners of the private equity funds, both in deciding whether to make the investment as they learn about what those strategies are and also as they themselves engage with their portfolio holdings. Again, that is very, very market-based.

Looking at things, I have to say that I work with money managers, and they are the most, "mathy," people in the world. They are the most green eyeshade, resolute, forward-looking people in the world. And portraying them as sort of flower-strewing hippies who vote on behavior, based on what their wishes are about flowers and bunnies is just not true.

Ms. WATERS. Based on the knowledge that you have about the position that these pension funds are in, perhaps we need some legislation to deal with that. Do you agree?

Ms. MINOW. I would love to see that. Thank you.

Ms. WATERS. Thank you, and I yield back.

Chairwoman WAGNER. The ranking member yields back. The Chair now recognizes the gentleman from Michigan, Mr. Huizenga, who is also the Chair of our Subcommittee on Oversight and Investigations, for 5 minutes.

Mr. HUIZENGA. Thank you, Madam Chairwoman, and I appreciate the panel. Welcome to the alternative universe.

It is amazing. Yesterday, this side of the aisle was compared to, "Trotskyites." By the way, the definition of that is socialist democracy. And by the way, Trotsky was trying to overthrow democratic capitalism, and he didn't think the Soviet Union was going far enough. We also had a misquoting of Milton Friedman yesterday. This month is the 50th anniversary of his seminal work. The social responsibility of business is to increase its profits. It is literally the name of his essay. But we are being told by others on the other side of the aisle that we are somehow anti-capitalist, anti-democratic. It is insanity. It is complete insanity and just underscores how political this has become.

I am going to get to the Index Act, Mr. Netram, first and foremost. Republicans in both the House and Senate introduced the Index Act, which highlights the roles some asset managers play in passive managed funds. You noted in your testimony that boards of directors must act in Main Street investors' long-term financial best interests, and those investors have the right to hold company leaders accountable via the proxy ballot. How important is it for

these shareholders to have an active role in the shareholder voting process? In other words, is it important that Congress create some guardrails on investment advisors who direct how shareholders should cast their votes?

Mr. NETRAM. It is critically important because these are not shares of the asset managers. These are shares held for the benefit of Main Street investors. They deserve to have a voice in that process.

Mr. HUIZENGA. Right. I want to move on to some of the other issues that we need to cover here. Proxy advisors like Glass Lewis and ISS—and the former president of one of those institutions is here today—affect the outcome of millions of shareholders' votes. Their influence is growing, and, unfortunately, they increasingly focus heavily on ESG initiatives without any accountability, oversight, or competition. That is why they will be appearing before my Oversight and Investigations Subcommittee this afternoon.

Mr. Berry, your testimony pointed to overlap between the environmental and social agendas and prominent shareholder activist and proxy advisors. How do proxy advisors and shareholder activists arrive at the same priorities? Do they coordinate?

Mr. BERRY. The short answer is, yes. They work through organizations like Climate Action 100+ that convenes asset managers, institutional investors, proxy advisors, and shareholder components.

Mr. HUIZENGA. Okay. And is it true that companies are already required by law to disclose, "impacts related to climate change that have a material effect on a company's business and operations?"

Mr. BERRY. Yes, absolutely, if material.

Mr. HUIZENGA. Materiality, materiality, materiality. Okay. Given that material information regarding climate change must already be disclosed, is there a good reason to deviate from that standard?

Mr. BERRY. As we said previously, it is a time-tested standard, and there is no good reason as far as ISS.

Mr. HUIZENGA. Okay. In ISS' written testimony, the firm states that ISS performs its work in a prudent, open, and honest manner. Yet, in December of 2022, the head of governance solutions for ISS testified that ISS failed to consult with the Texas Employees Retirement System over new types of shareholder proposals.

Mr. Berry, how does a failure like this and others affect the accuracy, reliability, and information provided to those actual shareholders?

Mr. BERRY. It can have a huge effect. If there is no feedback, there is no consultation. How can you expect reliability?

Mr. HUIZENGA. Okay. Mr. Netram, you emphasized in your testimony that proxy advisors have an outsized influence on corporate governance at manufacturers of all sizes, public and private. By the way, I know many privately-held companies that have sustainability officers because their customers requested it, or because they feel internally that they need to do that. How does this influence affect the decision-making process of companies and their boards?

Mr. NETRAM. For the manufacturing industry, proxy advisory firms operate as sort of quasi-regulators. Their influence is felt well before any vote is cast as companies try to contour themselves to

match their policies with proxy advisory firms' recommended policies.

Mr. HUIZENGA. And it is true that while those proxies or those shareholder proposals may not be legally binding, ISS and Glass Lewis will then recommend that those boards reject them or get voted out, correct?

Mr. NETRAM. That is correct.

Mr. HUIZENGA. Okay. Maybe not by legal act, but certainly by action. Okay, quickly—well, I guess I have 7 seconds left, so I don't know that I am going to be able to do this, but I hope that we can blend some common sense to this and that, "materiality," is the watchword, and I yield back, Madam Chairwoman.

Chairwoman WAGNER. The gentleman from Michigan yields back. I now recognize the ranking member of the subcommittee, the gentleman from California, Mr. Sherman, for 5 minutes.

Mr. SHERMAN. Capitalism is under attack. If by the sweat of your brow and the forbearance of consumption you accumulate capital and you have the courage to invest, these proposals would deprive you of the information that is material to millions and millions of investors. And if you do become a shareholder, the proposals here would prevent the shareholders from affecting the behavior of the company they own. The purpose here is to blind the investors when they make the investment decision and hog-tie them when they try to affect the company's behavior.

Today's Republican Party has recently begun this war on capitalism. As I said yesterday, they are of the same mind now with the centuries'-long effort of the Socialist Workers Party of Leon Trotsky. The gentleman from Michigan says that is unfair, and he is right because it is unfair to Mao Zedong because it takes a Eurocentric view of communist thought and fails to give appropriate mention to East Asian communism. Imagine a shareholder resolution that says the company must de-risk from China, decouple from China, and not sell advanced technology to China. Many boards, probably most, would fight hard to block that from the proxy statement, and two political parties will help them do that: the Republican Party of the United States; and the Communist Party of China.

We are told that we are supposed to protect retail investors, but we are told that if you have $25,000 to invest, you can propose something, but if 3 people have $10,000 to invest each, they can't. We must have aggregation. We shouldn't just be talking about ESG, ESG-WNC. The last hearing that I chaired of this subcommittee focused on workforce as part of ESG. And as I have just mentioned, we need resolutions about how companies deal with China, and we need disclosures of the big China risks that so many companies take. Mr. Berry tells us we should rely on States. That is a race to the bottom. When a State needs $100 million or even a few million dollars in revenue, they will allow boards to be entrenched management. I do agree with Mr. Berry that we should allow all flowers to bloom, both red flowers and blue flowers.

A lot of people on my side of this issue are not CPAs—I guess I am the only CPA on our side—and underestimate just how hard it is going to be to really have meaningful ESG disclosures. To ascertain, quantify, tabulate, define, make comparable, and audit nu-

merical information is very difficult to devise that system. We are told that investors who care about ESG are the fringe, and, as Ms. Minow points out, they are the winners.

Ms. Minow points out the importance of private companies, and that we need to require disclosures by multibillion-dollar companies, even if they are privately held, and not just to the private equity companies that invest. Mr. White puts forward the idea that if you want to be a, "John Denver investor," rather than an, "Ebenezer Scrooge investor," you are morally wrong somehow, or you are incompetent, or you should be blinded and hog-tied, and, frankly, I don't agree with that.

We are told that we have to prevent inaccurate speech. Everybody who wants to kill the First Amendment says that they are not going after good speech; they are only going after bad speech. The answer to bad speech is good speech. And we shouldn't be censoring political talk, and we shouldn't be censoring what advisors have to say.

Ms. Minow, we are told that somehow there is a big cost involved in these things. I remember when creating the proxy statement was very difficult because you had to set the type. We didn't have computers back then—I was at the financial printing office—but I would assume that printing something is easy now. Tabulating is easy. Isn't most of the cost here the cost of trying to prevent it by fighting this with lawyers and to prevent the vote from ever being proposed?

Ms. MINOW. Yes, that is true. As I said, the costs that they send out are very inflated. Shareholders are limited to 500 words. They can have as many words as they want to respond. They have in-house counsel to respond. In my opinion, it doesn't take more than an hour or two.

Mr. SHERMAN. So they attack it as being fringe, and they say it is expensive, and the expense is the money they get to prevent these fringe proposals from winning.

Ms. MINOW. Correct.

Mr. SHERMAN. I yield back.

Chairwoman WAGNER. The gentleman's time has expired. I now recognize the gentleman from Pennsylvania, Mr. Meuser, for 5 minutes.

Mr. MEUSER. Thank you very much, Madam Chairwoman. And I certainly thank all of our witnesses as well.

Proxy voting process is not working to serve the best interests of investors. I think that is kind of clear when you have 97 percent of the proxy voting held within two organizations, which would be alarming to, I think, general investors who probably aren't aware of that and don't engage in proxy voting as well. The idea that you happen to agree with a particular ideology from these proxy companies and that is why you are favorable to them, can really hedge it down a road that could reverse its course sometime in the future, particularly when laws, regulations, standard practices, laws that have been in effect since 1940, like the Investment Advisers Act of 1940, where there are fiduciary responsibilities, where there is ERISA, where it is very clear for pension funds and whatnot that you are to act in the interest of the investor, not an ideology, and if there is a conflict of interest, it shouldn't be disclosed, little

things like that, that have been followed for decades now. But instead, we have an SEC that has decided to put out a 500-page report that says, well, we are going to do things a lot differently now, and because we believe in a certain ideology, we are going to force—not recommend, not suggest, not even give tax incentive towards—but we are going to force investment companies.

And of course, we have seen pushback. Warren Buffett has called it, "asinine."—I think that is a technical term. Large investment firms—I will leave their names out—have stated that they are being asked, mandated, required, told to renege on their fiduciary responsibilities. So, what are we talking about here? If we want to see these sorts of changes, they need to go through an actual legislative body of the Federal Government called Congress, right? Not the whims of a few individuals who are temporarily going to be running a particular agency, such as the SEC.

Anyway, Dr. White, how does the polarization of business management, capital allocation, influenced by proxy advisors—go back to the proxy advisors—impact market confidence and invester trust? Do you think that this just breeds trust, this sort of mannerism of voting?

Mr. WHITE. Thanks for the question. When you think of the word, "trust," you trust whom you are investing your money with—your retirement income—that they are going to vote in your best interest as a shareholder. They have a fiduciary duty to do so. The reality is that asset managers can simply rely on the voting advice of proxy advisors whose interests might not be maximizing shareholder value. If I was rational, I would probably sort on only the votes that they recommend voting against for the board, and only the proposals on the ENS side of governance that they recommend voting for, and that leaves out informed voting, and it is why we see asset managers who conduct their own research tend to outperform. So, relying on proxy advice can erode that trust that your investment advisor is acting in your interest.

Mr. MEUSER. Thank you. Mr. Netram, what do you believe, and isn't it true that the information that is now being required by Chair Gensler's ESG disclosure proposals as material, if it is material to a public company's operations, wouldn't it already be obligated to be disclosed?

Mr. NETRAM. That is absolutely true. That is the core duty of a corporation here to disclose material risk to their investors so that they can make informed investing decisions. That duty currently exists with or without this proposed rule.

Mr. MEUSER. Okay. Mr. Netram, you mentioned Representative Steil earlier. I don't know if you alluded to the bill. Would you comment on the importance of his legislation?

Mr. NETRAM. Absolutely. Congressman Steil's bill would make sure that proxy firms are actually subject to some level of oversight. Right now, we are in a system where these are the only actors in the financial system that have minimal to no oversight at all. Everybody else—companies, exchanges, asset managers—are subjected to fairly significant oversight. Proxy firms so far have been able to escape that, and the Steil bill would bring them into the net.

Mr. MEUSER. Excellent. Thank you. Madam Chairwoman. I yield back.

Chairwoman WAGNER. The gentleman from Pennsylvania yields back. The Chair now recognizes the gentleman from Georgia, Mr. Scott, for 5 minutes.

Mr. SCOTT. Thank you, Madam Chairwoman. I appreciate that.

Ms. Minow, let me start with you. The shareholder process provides a very important mechanism for investors to express their views and is very essential to making sure that company executives are managing the company for the benefit of its owners, and that is what they are there for. However, I am very concerned that the SEC's recent proposal to amend Rule 14a-8 will create additional uncertainty and encourage the submission of proposals by proponents whose interests are not aligned with the interests of shareholders who are seeking a return on their investments.

For example, in a situation last month, SEC Commissioner Mark Uyeda raised concerns about the process through which the agency staff decides whether to allow companies to exclude shareholders' proposals from their proxy statements. And Commissioner Uyeda cited several figures that showed an 18-percent increase in the number of shareholder proposals submitted to companies between 2021 and 2023, and a 40-percent jump in the number of proposals that reached a vote over that same 2-year period.

My first question is to you, Ms. Minow. Do you agree with SEC Commissioner Uyeda that we have seen an increase in shareholders proposals over the past 2 years?

Ms. MINOW. Thank you very much, Congressman. Yes, we have, but as I have noted, a lot of those proposals are withdrawn following successful negotiations with the company. And, of course, we have had this new influx of anti-ESG proposals, most of which got single-digit numbers of support and cannot be resubmitted because the system works very well. That is how markets work.

Mr. SCOTT. Would you attribute this increase, in part, to the updated November 2021 guidance issued by the SEC's Division of Corporation Finance about the application of Rule 14a-8, and its decisions of whether to give no-action relief to companies that seek to avoid shareholders proposal being voted on?

Ms. MINOW. My understanding is that ruling is a return to earlier guidance. During the Trump Administration, a lot of tightening of those rules occurred, and I think that the general feeling of the investor community is a preference for the earlier approach.

Mr. SCOTT. And in your experience, do you know of any shareholder proposal that led to a negative change or a deterioration of a company?

Ms. MINOW. Thank you for that question. As I noted, even a 100-percent vote in favor can be ignored by the company, so that has not happened.

Mr. SCOTT. Thank you very much.

Ms. MINOW. Thank you.

Mr. SCOTT. I yield back.

Chairwoman WAGNER. The gentleman from Georgia yields back. The Chair now recognizes the gentleman from Arkansas, Mr. Hill, who is also the Chair of our Subcommittee on Digital Assets, for 5 minutes.

Mr. HILL. Thank you, Madam Chairwoman. I appreciate this hearing. And I'm glad to have our panel with us. Nell, it is nice to see you again. How long you have been working on these issues? I think I can beat you by about 2 years, but we have known each other a long time, and you have been a real voice in the corporate governance arena.

With that being said, I have to say I don't know if I share David Scott's concerns or not, but I will share his raising SEC Rule 14a-8, and I am not convinced that, as proffered, we are going back to the way things were before the Trump Administration's changes. We had a great hearing yesterday, and we heard a lot of concerns about this. And in my view, between Staff Legal Bulletins 14I, 14J, and 14K, replacing with this 14L, it is a problem. I think it really politicizes the proxy process.

And my friends on the other side of the aisle might be talking about great progressive ideas and things of that nature, and I don't think they should be met with conservative responses. It is a law of physics here that a force of equal might well be met by another one opposing it, and that is not what the proxy process is for.

And in addition to opening up to these social things, which is not relevant, it disconnects it from the individual company responsibility, and that is a big difference that usually doesn't get mentioned. So it makes it, as I say, much easier for politically-motivated people to weigh in on this situation. Take the wokest company on the planet, you pick it, Apple, Google, they reject every one of these social impact-type statements. The management, the board recommends it because it is not relevant to the mission. I think we need to go back to the future and be focused more about who is on the board. Are they competent? Compensation committees, are they independent? Are they implementing the strategy? Are they developing a good quality return for shareholders and getting out of all this madness?

Mr. Netram, let me start with you. Companies are facing more and more detailed ESG and political proposals that are intended to interfere or could be considered to be interfering with regular business operations. And 14L removed, as I noted, that longstanding commitment directly to the individual business by the way it is phrased. How does this proposal process change when the SEC limits no-action releases under Rule 14a-8, as Mr. Scott noted?

Mr. NETRAM. Thanks for the question, Congressman. Effectively, what it does is it gives activists a roadmap to engage in real micromanagement of the company. And as you noted, part of what we need to do here is to support companies taking risks and innovating and delivering returns to investors, and part of that is on the company itself. The company has a duty to respond to the marketplace. If a company isn't responding to the marketplace for the demands that they need, would the marketplace trust them to act and build their business? That company will wither and die, so taking the act of this and the roadmap out of it will allow companies to flourish.

Mr. HILL. Dr. White, when you look at these 14a-8 proposals, it seems like it tips the scale to special interest proponents on either side of the political spectrum. Would this increase litigation risk for

companies, and what other potential impacts might it have on corporate governance?

Mr. WHITE. Yes, thank you for that question, Congressman. It would certainly continue to tip the increase towards special interest groups. What we saw with 14L, which is a staff opinion, that is, something that receives commentary like proposed rulemakings at the Commission, we saw an increase in the SEC's disagreement for no-action relief requests by more than 50 percent. And we can expect that to continue with the new Rule 14a-8 proposals that came out in July 2022. The SEC added language that says even if you address the same subject matter in the same objective, if it is addressed through a different means, it is not a reason for duplicative exclusion. So, one could easily imagine four or five activists getting together and slightly tweaking the version of their proposal and having five proposals on the same topic appear on the proxy.

Mr. HILL. Yes, I just think that goes against the whole. We have so many rules against not doing that with owning stock, and yet we are going to try to manipulate the process through the proxy. It doesn't sound like a good idea.

Ms. Minow, we have been around each other a long time on passively-managed funds. That was an innovation when we were in business together. Now, it dominates the market. Do you think that a passively-managed ETF proxy should just default to vote with management as a fiduciary in that capacity, except maybe in the case of M&A?

Ms. MINOW. No, I don't. As we said——

Mr. HILL. Why?

Ms. MINOW. ——before, the proxy advisors, over 90 percent of their recommendation——

Mr. HILL. Not the proxy advisors.

Ms. MINOW. I understand that, but——

Mr. HILL. Respond to me off the dais. My time has expired. It is not about the proxy advisors; it is about what the management is doing. I yield back.

Chairwoman WAGNER. The gentleman from Arkansas' time has expired. The Chair now recognizes the gentleman from California, Mr. Vargas, for 5 minutes.

Mr. VARGAS. Thank you very much, Madam Chairwoman, and I appreciate the opportunity. And again, I thank the ranking member, and, of course, I especially thank the panel here today. I seldom agree with my colleagues, but today I do. Welcome to the alternative universe. This is insanity, complete insanity. I agree with those statements.

This was the headline that I read this morning in The Washington Post, "Floods, Fires and Deadly Heat Are the Alarm Bells of a Planet on the Brink," an article by Sarah Kaplan. It reads, "The world is hotter than it is been in thousands of years. It is as if every alarm bell on the earth were ringing. The warnings are echoing throughout the drenched mountains of Vermont where 2 months' worth of rain fell in only 2 days. India and Japan were deluged by extreme flooding. They are shrilling from the scorching streets of Texas, Florida, Spain, and China, with a severe heatwave also building in Phoenix and the Southwest in the coming days. They are burbling up from the oceans where temperatures have

surged to levels considered beyond extreme, and they are showing up in unprecedented, still-burning wildfires in Canada that have sent plumes of dangerous smoke into the United States.

"Scientists say there is no question that this cacophony was caused by climate change or that it will continue to intensify as the planet warms. Research shows that human greenhouse gas emissions, particularly from burning fossil fuels, have raised the earth temperature by 1.2 degrees."

It goes on to explain that this is insanity.

When we are trying to take away the rights of shareholders to know about these climate disasters, and we are doing it in the name of shareholder rights, this reminds me of the quote from Peter Arnett back in the Vietnam era, who said, "It became necessary to destroy the town to save it." It is often misquoted as, "We had to kill them to save them." This is what we are trying to do to the shareholders here. This is exactly what we are attempting to do. This is insanity. Shareholders want to know about this. Investors want to know about this, their long-term profitability.

Ms. Minow, am I wrong about this? Is this fringe?

Ms. MINOW. Thank you very much. Congressman, I appreciate that, and it allows me to mention that what we are seeing in these large institutional investors is a portfolio-wide approach. And that is, I think, a much better approach for sustainable, long-term wealth creation, than trying to do stock picking. You are 100-percent right. These issues that you are talking about affect every company in America. The information that we are asking for—it is no secret that it is the fossil fuel industry that is against these questions. Everybody else is for them. I haven't noticed anybody come up with a single example of some ESG proposal or ESG vote that was somehow detrimental to anybody. There are a lot of grand statements, but very few specifics.

Mr. VARGAS. I totally agree. It is fascinating that when I talk to people, this is their huge concern, especially in Phoenix right now, when they are going to San Diego because we can't take the heat. This is information that they want their investors—go ahead?

Ms. MINOW. Yes, if I may make one more comment?

Mr. VARGAS. Sure.

Ms. MINOW. I am old enough to remember when I heard a lot of complaints about the short-termism of the large institutional investors. They only care about the next quarter. Now they are looking into the future, they are looking into the long term, and we are getting the same complaints from the same people. You can either have patient capital or silent capital. You cannot have both.

Mr. VARGAS. And it is interesting to me, again, when shareholders want this information, where they find it material, that now my good friends on the other side of the aisle say, "You don't get to have this information. We are not going to allow it." I don't know how that is free market—I won't quote Trotsky or Mao Zedong, but it does seem to me that it goes against capitalism. It just seems to be going in the wrong direction. I don't have much time here left other than to, again, thank the panel for being here. I appreciate it. It has been very lively, but read the headlines, and talk to the people at home. You know that climate disaster is what is on their minds, especially during these heatwaves, and during

the smoke coming from Canada that we have never seen before. I don't know how the hell this isn't material. With that, I yield back.

Chairwoman WAGNER. The gentleman from California yields back. The Chair now recognizes the gentleman from Oklahoma, Mr. Lucas, for 5 minutes.

Mr. LUCAS. Thank you, Madam Chairwoman. And before I focus on my questions, I would simply note I have just come from a House Science Committee hearing, and I would suggest to my colleagues, both in Congress and around the country, that one of the keys to addressing the future of this great planet and the issues that we address here from a business perspective is changing how we create our energy sources, urging the bipartisan leadership, the bicameral leadership, the appropriations process to fully fund fusion research so that we can go to the next generation of energy production for this planet. We have to focus on that. If we won't spend time and resources on the next source, well, that is our fate.

Let me pull back closer to home. In November of 2021, the SEC issued revised guidance aimed at broadening the scope and increasing the volume of shareholder proposals to be considered by public companies. Instead of focusing on how social policy matter might impact the actual business, these proposals can now take aim at the wider aspects to society unrelated to specific business issues.

Mr. Netram, from your understanding, how does the SEC staff determine if an issue has a broad social impact? Who gets to play God on that one?

Mr. NETRAM. That is an excellent question. It raises a number of questions, the guidance. What is the society that we are looking at? Is that the locality in which a company operates? Is it the entire United States? Is it the entire world? What is an impact? What is a measurable impact? Who is being impacted, and has Congress actually empowered the SEC to make those decisions?

Mr. LUCAS. Mr. Berry, could you also discuss this?

Mr. BERRY. Certainly, there is a tremendous amount of viewpoint bias that the SEC staff exercises here, and they will call one thing significant and another insignificant on pretty nakedly political grounds.

Mr. LUCAS. In your observations, does there need to be any relationship to the operations of the company to get one of these classifications?

Mr. BERRY. Really, the upshot of what the SEC said in 14 hours is there doesn't need to be any tie whatsoever.

Mr. LUCAS. Oh, my goodness. Mr. Berry, in your written testimony, you provide historic context to how the SEC requires public companies to interact with shareholders. Could you expand on this historic perspective, specifically how the SEC arrived at the current treatment of shareholder proposals, and how this position has changed over the past decades?

Mr. BERRY. The SEC originally focused its rulemaking on the core mandate of disclosure, what Congress directly authorized. But over the decades, the SEC has gotten more into the substance of corporate governance, something that the courts have disfavored, and yet we are still here. In the last few decades, the SEC has essentially opened the gates to all manner of shareholder proposals in the EMES space.

Mr. LUCAS. Kind of following up on that, Mr. Doyle, also looking at the historic perspective, can you discuss how the proxy process has evolved from, say, the mid-1900s to where we are today?

Mr. DOYLE. The process itself?

Mr. LUCAS. Please.

Mr. DOYLE. Yes, sort of. Again, as I think has been mentioned by a couple of other witnesses already, it has developed—I will try to come up with the right term here. As was mentioned, it was first not talked about through the Security and Exchange Commission, and then, as mentioned, they started to provide rules for their involvement. And I will mention that the more recent issue with proxy advisors is their inherent bias on both the recommendations that they make for clients that they have as well as for for whom they have consulting services. I don't know if that answers your particular question.

Mr. LUCAS. Fair point. The SEC's aggressive rulemaking agenda is set to inundate investors with a flood of non-material information that public companies are required to disclose.

Mr. Netram, could you speak to the challenges and compliance costs that public companies face and how they are preparing themselves for this? This is not free, right?

Mr. NETRAM. It is absolutely not free. There is a dollar cost associated with responding to these proposals, but really, the larger cost and the bigger impact to the investors that companies are supposedly serving is the distraction from actually focusing on the underlying business. Manufacturers are facing an increased challenge. We have supply chain constraints, workforce constraints, competition from China, and raw material constraints, and taking time and attention away from that to respond to activists is really instrumental.

Chairwoman WAGNER. The gentleman's time has expired.

Mr. LUCAS. Thank you, Madam Chairwoman.

Chairwoman WAGNER. The gentleman from Oklahoma yields back. The Chair now recognizes the gentleman from Illinois, Mr. Casten, for 5 minutes.

Mr. CASTEN. Thank you, Madam Chairwoman. And thanks to all of our witnesses, and I want to thank you for coming here today and give you a little respite from financial services.

We are all now going to travel to an episode of Shark Tank. Congratulations, you are all billionaires, and I am an entrepreneur with a great idea I would like to pitch to you. But as a pre-condition of the pitch, I get to be CEO of the company we are going to build, and I do not have to listen to any of your nonsense as I deploy your capital or make hiring decisions. Are any of you interested in hearing my pitch? Are you interested in signing that term sheet?

Ms. MINOW. No.

Mr. NETRAM. I would like to hear the pitch.

Mr. CASTEN. You are a weirdo.

[laughter]

Mr. CASTEN. I frame it that way because it is blindly obvious to the average American how Shark Tank works, what the rules are, and I think we can get caught up in a lot of this language around shareholders. But let me remind my colleagues, as I did yesterday,

of Milton Friedman's theory of shareholder primacy which says that corporate executives are employees of corporate owners and are accountable thereto.

If you want to know what happens, if you can ignore the interests of shareholders, if you can get money and not have to be accountable to them, I would remind our colleagues of the hearing not that long ago with John Ray and the FTX bankruptcy. And let's ask Sequoia and Citadel what they thought about signing term sheets where they had no authority to impact how capital was spent. Milton Friedman is turning over in his grave, but I am sure that our nation's beleaguered C-suite executives are thanking the Republican Party for standing up for their fragile interests and needs.

Mr. Netram, do you believe that companies' climate risks are material information for investors to know, yes or no?

Mr. NETRAM. I'm sorry, sir. Can you repeat the question?

Mr. CASTEN. Do you believe that the climate risks of a company represent material information that investors should know?

Mr. NETRAM. I think it depends on the underlying company and what business risks that they face.

Mr. CASTEN. Okay. I think you used the word, "material," 29 times in your testimony. Are you familiar with the definition of, "materiality," that guides the SEC?

Mr. NETRAM. Yes, sir.

Mr. CASTEN. Okay. And just to remind everybody, I will read it here. It was from the *Basic Inc.* v. *Levinson* Supreme Court case: "Information is material if there is a substantial likelihood that a reasonable shareholder would consider it important in making an investment or voting decision, or if it would have significantly altered the total mix of information available," a reasonable investor, not what certain Members of Congress think a reasonable investor should do, because I know more than them what is reasonable.

In 2016, the SEC issued a concept release requesting comment on existing disclosure agreements out of the JOBS Act. Do you know what percentage of investors commented to say that the voluntary reporting was inadequate to meet the demand for climate-related information?

Mr. NETRAM. I do not.

Mr. CASTEN. It was 90 percent; 90 percent of investors said voluntary reporting is insufficient. Do you know on the current proposed climate disclosures what percentage of investors have commented in support of climate disclosure and public company 10ks?

Mr. NETRAM. I do not.

Mr. CASTEN. It's 97 percent. This debate is settled. There is no question about whether climate disclosures are material unless you think that there are people on this committee who know better than free markets, who know better than the interests of investors.

The SEC's mandate, I would remind everybody, is to maintain fair, orderly, and efficient capital markets and to facilitate the formation of capital. It is not to protect C-suite executives. We are here to protect capital markets. We are here to protect free markets. It may hurt my colleagues' feelings to be compared to the socialists and communists of lore, and I have tremendous respect for the bipartisan Senator. I did not misquote Milton Friedman yester-

day, but I am going to misquote Barry Goldwater today, "Partisanship in defense of free markets is no vice." And I am sorry that it has become partisan to look out for the interests of investors, to look out for competitive markets, to make sure that we do not end up with a capital market full of FTX's where you get a bunch of dumb money where executives can do whatever they want.

And I get it. There are people who would like that in this world. Our obligation in Congress is not to look out for them, and I need you all to be full-throated and join us and do that because if we do not, this beautiful, wonderful economy we have is dead. I cannot believe we are having this conversation. I yield back.

Chairwoman WAGNER. The gentleman yields back. The Chair now recognizes the gentleman from Wisconsin, Mr. Steil, for 5 minutes.

Mr. STEIL. Thank you very much, Madam Chairwoman. I appreciate you holding today's hearing. I think it is absolutely essential that we have this conversation, in particular when we see the massive concentration between ISS and Glass Lewis as it relates to proxy advisors and their advice, which is sometimes pretty suspect. Sometimes, we see them get the facts wrong. Sometimes, they even get the name of the CEO wrong in some of their information.

If I can start with you, Mr. Netram, is there a reason we shouldn't be able to see the analytical process that is playing out by these two proxy advisors that have a pretty clear duopoly on the advice?

Mr. NETRAM. I'm sorry. Can you repeat that question?

Mr. STEIL. Sure. They are providing information, but we don't have visibility into the methodologies that these proxy advisors are using. Should we have visibility into the methodologies that these two proxy advisors are using?

Mr. NETRAM. Absolutely. We need to have visibility into the methodologies, their sources of information, and their conflicts of interest.

Mr. STEIL. I think that is essential. Do you agree, Mr. Doyle?

Mr. DOYLE. I do.

Mr. STEIL. Mr. Berry?

Mr. BERRY. Absolutely.

Mr. STEIL. It seems like it should be absolutely essential. It seems like a bit of a no-brainer. And then, we have Chairman Gensler striking down the original proxy advisor rule that was drafted when Chairman Clayton was there. Do you know what the rationale would be behind that, Mr. Netram?

Mr. NETRAM. I believe that the rationale was to reverse the Clayton-era changes, thinking that they gave too much power to companies.

Mr. STEIL. But really what we are doing is allowing ISS and Glass Lewis to be completely unaccountable. Is that correct?

Mr. NETRAM. Absolutely. It is really——

Mr. STEIL. So really, the net effect of Chairman Gensler's decision was to actually allow these two entities to be able to operate in the dark with no oversight from the Federal Government as they are providing advice. But we have seen them provide advice in conflict either with law or in the case of just simple errors without an

ability for companies to be able to simply come back and counter the information that is being provided. Is that correct?

Mr. NETRAM. That is correct.

Mr. STEIL. Do you agree with that, Mr. Doyle?

Mr. DOYLE. I do.

Mr. STEIL. Mr. Berry?

Mr. BERRY. Yes.

Mr. STEIL. What is the impact, Mr. Berry, when you allow this duopoly to play out when misinformation is being produced or information that simply needs to be countered because one of the proxy advisors views it in the best interest of a company for that company to engage in illegal behavior, for example, the Travelers case where a proxy advisor recommended in favor of a shareholder proposal which would have required Travelers, in that case, to engage in illegal behavior by altering the price of insurance based on race, which is outlawed in our States, rightfully so.

Mr. BERRY. Yes. Inadequate oversight of the proxy advisors means they are going to be giving the store away to shareholder activists to drive all kinds of behavior, including things that can be illegal.

Mr. STEIL. Mr. Netram, do you agree with that?

Mr. NETRAM. I agree, yes.

Mr. STEIL. And what is the solution to this, Mr. Netram? I have a bill—you have commented on it previously—that actually allows us to shine some light, to have some disclosure, some understanding, some oversight over this duopoly. Do you think that is an appropriate approach?

Mr. NETRAM. I think legislation is desperately needed here to bring some transparency to this process.

Mr. STEIL. What do you think the key aspects of that transparency should be?

Mr. NETRAM. I think there are two keys. The first is disclosing conflicts of interest, disclosing methodologies, disclosing their sources of information so that investors can see exactly what is going on here. And then second, making sure that the anti-fraud standards actually apply to proxy advisory firms.

Mr. STEIL. Making sure that what standards?

Mr. NETRAM. The anti-fraud standards.

Mr. STEIL. Absolutely. There should be some accountability to ISS and Glass Lewis if they are engaged in providing advice that is either misleading and correct or, in the case of Travelers, illegal. Is that right?

Mr. NETRAM. That is correct.

Mr. STEIL. And does the legislation that I have put forward accomplish that goal, in your opinion?

Mr. NETRAM. It absolutely does.

Mr. STEIL. Mr. Berry, do you have any further comment on that?

Mr. BERRY. I think if we cut down on the agency problems with the proxy advisors in the same way we care about agency between shareholders and managers, that would be a huge improvement.

Mr. STEIL. So, we should disclose conflicts of interest?

Mr. BERRY. Absolutely.

Mr. STEIL. And do you see conflicts of interest in the two largest proxy advisor firms?

Mr. BERRY. Yes, especially between consulting and proxy advice, there are real issues there.

Mr. STEIL. Mr. Doyle, I see you nodding your head. Do you agree with that?

Mr. DOYLE. I do, and I would also mention that members on this committee and others have supported through a bipartisan way to respond to and to try to alleviate some of those conflicts.

Mr. STEIL. I think, at a minimum, we should have disclosure. I think it is abysmal that Chairman Gensler struck down the Clayton rule. I think it moves us away from further disclosure. It allows these two proxy advisors to operate in the dark. I think we actually need to have a more robust regime than was even the rule in place. I appreciate you being here and your testimony today. Madam Chairwoman, I yield back.

Chairwoman WAGNER. The gentleman from Wisconsin yields back. And the Chair now recognizes the gentleman from Massachusetts, Mr. Lynch, for 5 minutes.

Mr. LYNCH. Thank you, Madam Chairwoman. I also thank the ranking member and I appreciate the good work of the panel.

Ms. Minow, prior to coming to Congress, I served as a union trustee on the Iron Workers Pension Fund, the Taft-Hartley Fund. I was a union trustee, and we would hire asset managers and obviously rely upon proxy vote services as well, advisors. And I have to say that as a union trustee, if a fund manager or an asset manager and proxy advisors ever voted against the interests of the ironworkers and the participants of that fund, they would be former fund managers, former asset managers, former advisors.

Some are painting this as a system with no accountability and that it is a couple of activists that are directing the votes here. Is that really what is happening, or is there some level of, dare I say, democracy and causation between the views of the participants of these funds and the way the proxies are voted?

Ms. MINOW. Thank you, Congressman, for that question. It has been my great privilege to conduct training sessions for new trustees of union pension funds on proxy voting, and I have found them to be extremely interested in these issues for the protection of the plan participants. What do we all want? We want them to be able to retire in a comfortable way.

So, you are 100-percent correct that the union's pension funds and the other pension funds that I have worked with, the public pension funds primarily, are particularly focused on making sure that their asset managers make, buy, hold, sell, vote, and litigate any decisions about share ownership purely for the benefit of plan participants. Furthermore, the Federal Government has not only the authority but the obligation to act if they don't do it, and they have acted, not as often as they should, but they have acted in those cases.

I want to mention that it is not union pension funds or any other institutional investor who has called for non-financial measures of corporate performance. It is the Business Roundtable, which announced that they wanted to go for stakeholders, and they wanted to have this very amorphous idea of, throw the dart at the wall and then draw the target around it. So no, you are 100-percent correct.

Mr. LYNCH. Thank you. Madam Chairwoman, I ask unanimous consent to enter into the record a report by the Independent Shareholder Services entitled, "U.S. Shareholder Proposals Jump to a New Record in 2023."

Chairwoman WAGNER. Without objection, it is so ordered.

Mr. LYNCH. Thank you, Madam Chairwoman, and it is dated May 24th, so it is about 6-weeks-old, but in the takeaway section, it says that the volume of shareholder proposals has indeed jumped 14 percent between January 1, 2023, and May 31, 2023. Interestingly, it says this increase is being driven by a new wave of anti-ESG sentiment, fueling a record number of shareholder proposals. So you are right, there is a spike in proposals, but it is from anti-ESG people who are offering these shareholder proposals. And I have to admit, it looks a lot like democracy, right?

Ms. Minow, you have people who are arguing to protect the earth from climate change, and then you have people who are saying, we don't believe in that, and we don't invest along with those ideas. That is sort of the position we are in, right? We represent close to 800,000 people apiece, and if we don't listen to them, they will make changes in leadership. Isn't this a lot like democracy?

Ms. MINOW. It is exactly like democracy, and as I noted, most of the anti-ESG proposals failed to get enough to pass the threshold to be reintroduced, so that shows that the market works. Democracy works. One thing I love to tell Members of Congress is that even one vote is enough to elect a corporate director. So if 99 percent of the shareholders vote against, I will give you all shareholder proposals. I will get rid of shareholder proposals entirely if shareholders can vote out boards of directors. If you need 50 percent in order to serve on the board, then let the shareholders send the message that way. In the meantime, shareholder proposals are a very modest, low-cost way for them to raise the issues they care about.

Mr. LYNCH. Thank you. Madam Chairwoman, I yield back.

Chairwoman WAGNER. The gentleman from Massachusetts yields back. The gentleman from New York, Mr. Garbarino, is now recognized for 5 minutes.

Mr. GARBARINO. Thank you, Madam Chairwoman. Thank you so much for holding this hearing, and thanks to the witnesses for being here today.

Mr. Berry, we are pleased to hear that those across the aisle are concerned with shareholder democracy. In the spirit of promoting shareholder democracy, would you agree that if a shareholder proposal is rejected time and time again by a majority of shareholders, their voting preferences should be heard, and there should be a cooling-off period for it being resubmitted?

Mr. BERRY. Yes.

Mr. GARBARINO. Thank you very much.

Mr. Netram, in the spirit of promoting shareholder democracy, should two proxy advisory firms be able to dictate 30 percent of proxy votes? Shouldn't the shareholders themselves be voting and not auto-voting the preferences of third parties?

Mr. NETRAM. I believe the shareholders themselves should be voting for the preferences.

Mr. GARBARINO. Thank you. It has been suggested, Mr. Netram, that the cost of shareholder proposals is just an hour of work. Can you discuss the cost to companies?

Mr. NETRAM. Sure. The real cost to the companies lies in the time and attention that executives are diverting from the operation of the underlying business. In the manufacturing sector, in particular, we are facing a set of challenges that are existential, and taking the executives' attention away from that and navigating these incredibly turbulent waters is not helpful to shareholder value creation.

Mr. GARBARINO. Just an hour of work, that is not true. It is going to take a long time. What about retail investors? Is there a cost to them? Presumably, they have to read through the proposals to make informed decisions. Some companies have millions of retail investors. Is that time quantifiable?

Mr. NETRAM. It must be quantifiable. I don't know what the answer is, but I am sure that it is.

Mr. GARBARINO. Wouldn't making our markets more efficient and letting boards focus on sound financial policy rather than political platforms enhance capitalism?

Mr. NETRAM. I strongly agree with that statement.

Mr. GARBARINO. Thank you. I want to ask you now about impacts to the changes to Bulletin 14L. Companies are facing more and more detailed environmental, social, and political proposals that are intended to interfere with regular business operations. One publication that has helped fuel this pattern is the SEC's Staff Legal Bulletin 14L, which made a number of changes that broaden the scope of what could be deemed eligible for a company's proxy statement. One of those changes is the altering of ordinary business exclusion, effectively removing the longstanding requirement that there be a connection between a proposal and the company.

Mr. Netram, how does the shareholder proposal process change when the SEC limits the availability of no-action relief under Rule 14a-8? Additionally, how can this change interact with the operations or business of a company?

Mr. NETRAM. It fundamentally alters the way in which a business is run. If you remove that nexus between the core operation of the business and the shareholder proposal to open that up to really anything under the sun, you are taking the time and attention away from running your underlying business.

Mr. GARBARINO. Yes. You said you could open anything up under the sun, which means you could allow shareholders to influence more of the day-to-day operations of a company, right?

Mr. NETRAM. That is correct.

Mr. GARBARINO. Can you explain how the increased level of detail and specificity in shareholder proposals creates governance risks by distorting a board's decision-making process?

Mr. NETRAM. Absolutely. I think it goes beyond distorting the decision-making process to actually giving greater power to shareholder activists, in that under the new regime, you are allowed to make minor alterations to a proposal, infinite versions of alterations to proposals, and have corporate management be forced to consider each of those in turn.

Mr. GARBARINO. Is there any way to reform Rule 14a-8 to combat the submission and resubmission of non-germane shareholder proposals?

Mr. NETRAM. Yes. I think we need to go back to actually ensuring that proposals that are germane to the underlying business are the focus.

Mr. GARBARINO. Dr. White, the SEC's proposed amendments to Rule 14a-8 would tip the scales in favor of a small group of like-minded shareholders whose objectives may not be aligned with the objectives of mainstream investors or the best interests of the company and shareholders. Can you discuss the SEC's proposed amendments and the potential impact they will have on the public markets?

Mr. WHITE. Thank you for that question. Yes, there were three proposed amendments. One was the substantial implementation exclusion, and it says that if you have already substantially implemented the subject matter with the same objective and the same means, then you can exclude it. The new rules would require that you prove that in order to achieve that exclusion.

The duplication exclusion I mentioned earlier, which is if you have two or three activist shareholders that want to achieve the same objective, they can propose two or three different means, and it can appear on the proxy. For example, Amazon had 18 shareholder proposals on its proxy this year. If these rules were to move forward, it would make it even harder to remove.

Mr. GARBARINO. I am out of time. Thank you, Madam Chairwoman. I yield back.

Chairwoman WAGNER. The gentleman from New York yields back. The Chair now recognizes the gentleman from New York, Mr. Meeks, for 5 minutes.

Mr. MEEKS. Thank you, Madam Chairwoman. Ms. Minow, do proxy firms proactively push ESG-related information out to the investors, or is it customary for investors to ask for ESG-related information about a company as part of their established proxy voting policies?

Ms. MINOW. Thank you for that question. There is a variety—the clients have different relationships with ISS, and you have some in each of those categories. But I was one of the co-founders of ISS, so I can tell you that ISS began because all of a sudden there were complicated issues on proxies. Before that, it was all very routine: vote for the directors; vote for the auditor; go home. But all of a sudden, there were complex issues that had to do with CEO pay, that had to do with management entrenchment. And when the proxy advisors began, they started addressing those issues. Some will go to ISS and say, here are our policies, please vote according to our policies. Some will say, we will look at your advice, and we will evaluate it and decide what we agree with and what we don't agree with, so different clients have different kinds of relationships with ISS.

Mr. MEEKS. Would you say then, in asking these questions, is it unnecessary or irrelevant for an investor to ask for different kinds of information?

Ms. MINOW. Absolutely. That is required by their obligation as fiduciaries, and just as they get information about buy/sell deci-

sions, they are getting information about voting decisions and then acting on it according to their own policies.

Mr. MEEKS. Let me make sure that I am correct—would it be correct to say that proxy advisors are providing this information in response to a market-driven, investor-driven demand?

Ms. MINOW. That is 100-percent correct, and as I pointed out earlier, Presidential candidate, Vivek Ramaswamy, has now started an anti-ESG proxy advisory service, and anyone who wants to purchase that service can do so.

Mr. MEEKS. When we look at our capital market systems, which I believe to be the envy of the world—everyone looks at it, this is the envy of the world—it seems that for it to work best, we would want our institutional investors to have access to independent analysis provided by proxy advisors or any other source of their choosing to enable them to make the most informed decisions possible. Do you agree?

Ms. MINOW. One hundred percent.

Mr. MEEKS. So, why in the world do you believe that my colleagues on the other side of the aisle want to stifle this access?

Ms. MINOW. They want to kill the messenger, and that is the opposite of what capitalism and efficient market theory is about.

Mr. MEEKS. Kill the messenger. I don't understand that. I listened to my other colleagues when they were asking their questions. We are in some weird times here. Ms. Minow, shareholder proposals are helping to raise industry standards for the diversity of corporate boards and C-suites. Do you believe this is an effective way for shareholders to signal that they care about the diversity of a company's board or C-suite?

Ms. MINOW. I really want to emphasize your use of the word, "signal," because it is exactly appropriate. This is an area where shareholders are communicating. They are not forcing anybody to do anything. It strikes me that we literally pay these executives the big bucks so that their knees don't get weak when someone criticizes them.

Mr. MEEKS. Can you share examples from your work where shareholder proposals have led to positive changes or improvements within the companies?

Ms. MINOW. Absolutely. They have led to boards being far more engaged, and effective, and qualified. They have led to the end of many entrenching devices that made companies less accountable. As I said before, I am not saying anything good about CEO pay. I am just going to say it would be a lot worse if it were not for shareholder input. I think it has led to some very important changes and better disclosure, more accountability, and, again, that is what markets are all about.

Mr. MEEKS. Thank you. My time has expired. I yield back.

Chairwoman WAGNER. The gentleman from New York yields back. The Chair now recognizes yet another gentleman from New York, Mr. Lawler, for 5 minutes.

Mr. LAWLER. Thank you, Madam Chairwoman. Like many of my colleagues here today, I have serious concerns about the potential consequences of focusing on costly non-material environmental, social, and political issues at the expense of sound financial policies, what we are seeing in this press from both government regulation

and shareholder activism driving up the costs and burdens associated with participating in the United States public markets. And it detracts from companies being able to raise capital and foster economic growth. Instead of focusing on running their businesses, we see companies having to spend their time and resources addressing politically-motivated proposals that don't have anything to do with the company's strategic direction or long-term goals.

My home State of New York has been at the forefront of promoting ESG policies. Back in 2019, New York State Comptroller Tom DiNapoli released guidelines on how the New York State Common Retirement Fund would begin to pursue ESG goals with a new climate action plan, for instance. We have seen the Common Retirement Fund repeatedly filing shareholder proposals and pressing public companies to adopt these policies. This is not just some random shareholder. This is an elected official using his perch to drive companies to make decisions. That is not democracy, not even close. Over the past years, this fund alone has filed hundreds of proposals, and many companies have chosen just to settle and cut a deal, leading to more reports, and disclosures, and diverted resources.

This is the same pension fund, by the way, that just announced a negative return of 4.1 percent for the State fiscal year that just ended. Bang up job. They are doing good by the taxpayers because, by the way, in New York, the taxpayers are on the hook when we don't meet our requirements. Several pension funds in New York City are even facing lawsuits alleging that they have breached their fiduciary duty. Yes, this is really working out great. Good policies.

We have seen a lot of examples recently, and I hear it from my constituents. People want corporations to leave politics at home and focus on the underlying purpose at hand of running their businesses, selling their products, and delivering a return for their investors. Stay the hell out of politics. Leave it to Congress. Leave it to State legislatures. There are plenty of politics around here at all times. The American people are so tired of politics consuming everything from the media, to corporate America, to education. It is pathetic, and it is creating a challenge across-the-board.

Mr. Berry, do you agree that politics and social policy should be made in Congress and State legislatures and not in corporate boardrooms?

Mr. BERRY. That is what Congress and legislatures are for, Congressman.

Mr. LAWLER. I agree.

Mr. Netram, shareholders who submit proposals, especially on environmental and social topics, often argue that these proposals serve the long-term economic interests of companies and shareholders. Could you respond to this claim?

Mr. NETRAM. I would say that the long-term economic interests of shareholders are best served when companies focus on their underlying business itself.

Mr. LAWLER. Would you agree that if, for instance, the New York State Pension Fund is giving a negative return, that is probably not in the best interest of pension fund recipients?

Mr. NETRAM. Without knowing much about the New York City Pension Fund, those don't sound like great facts there.

Mr. LAWLER. That makes sense.

Dr. White, can you speak about how the prevalence and persistence of socially-oriented shareholder activism and the influence of proxy advisory firms affects shareholder value and the ability of corporations to make efficient and effective business decisions?

Mr. WHITE. Yes. Thank you. I have heard a lot of discussion today about how it may be taking 1 hour to respond to shareholders. You would get a low grade in my class if you submitted that as a response. You have to carefully consider each proposal, potentially negotiate with the special interests, request relief from the SEC, which they reject more than 50 percent of the time, and reply if they fail to provide relief. Amazon had 116 pages and 40,000 words, which would take the average investor 2 hours to read, so I doubt it would take you 1 hour to respond, if it takes you 2 hours to read, and was very politicized.

Mr. LAWLER. Thank you. I yield back.

Chairwoman WAGNER. The gentleman from New York yields back. The Chair now recognizes the gentleman from Missouri, Mr. Cleaver, for 5 minutes.

Mr. CLEAVER. Thank you, Madam Chairwoman. Ms. Minow, I thank you and all of our witnesses for giving of your valuable time to be here with us. I think we sometimes take for granted those of you who come before us and spend a lot of time. And the check we give you is very little, probably like zero, so thank you very much.

Saying something is so, does not make it so, and there are and have been here today suggestions that proxy advisors have their own political and social agendas. And many of those who have asserted that say that they have an outsized care about climate change, which I am still struggling with since this is the only climate we have. What are your views on this? Do proxy advisors always recommend in favor of climate or social proposals?

Ms. MINOW. Thank you for the question. And as Dr. White pointed out, there are a lot of shareholder proposals relating to climate which did not get substantial votes, and which got votes lower this year than they did in previous years. So no, that is not true.

Proxy advisory services, I will say it again: No one has to buy it. The people who do buy it are the most sophisticated, professional financial experts in the world. And they have a choice of one that is a registered proxy advisor, and one that is not, one that has conflicts of interest, and one that does not, and now a new one that is the anti-ESG. Maybe, they will get all three and compare what their recommendations are; those are their own financial choices. So yes, the evidence shows that the clients of the proxy advisors depart from the recommendations of the proxy advisors on any issue that is complex or controversial.

Mr. CLEAVER. Do you agree, Mr. White?

Ms. MINOW. I beg your pardon?

Mr. CLEAVER. I was asking Mr. White if he agreed.

Mr. WHITE. I think that sounds like a fair description of the proxy proposal process. Proxy advisors do have conflicts of interest. Some of them do not. I would be concerned, though, of such a con-

centration in two entities that have so much power. I think if we were describing any other setting where an entity influenced trillions of dollars of investment returns and we did not have oversight or regulation or transparency, we would be highly concerned, so I am not sure how proxy advisors are different.

Mr. CLEAVER. But neither of you are suggesting that the proxy advisors are puppet masters who have control over asset managers or institutions?

Ms. MINOW. I compare them to restaurant critics. You can read the review of a restaurant and decide, well, they don't like green peppers, but I do like green peppers, maybe I will like it. These are First Amendment-protected publications that are voluntarily purchased, and I would be very, very cautious about providing any kind of prior restraint or additional review.

Mr. CLEAVER. Great example with the restaurants. I don't like green peppers either.

Madam Chairwoman, I yield back.

Chairwoman WAGNER. The gentleman from Missouri yields back. The Chair now recognizes the gentleman from Iowa, Mr. Nunn, for 5 minutes.

Mr. NUNN. Thank you very much, Madam Chairwoman, and I thank the ranking member as well. I appreciate it, and I thank the panel very much for being here today.

I want to talk a little bit to our witnesses who are shedding light on this, I think, very important topic. People in my district, Iowa's 3rd, elected me to serve their best interests, not that of any political party or social agenda that is being set forward. To that end, I, along with my colleagues on both sides of the aisle today, support policies that prioritize protecting everyday families, farmers in my home district, small business owners, and Americans across-the-board. Their investment and their financial futures often depend on the decisions that are being made in this room. This follows up on yesterday's hearing on what we would like to drill down on for a term called, "robo-voting." This is an alarming and ramping process that has come up.

For those of you watching back in Iowa, robo-voting is the practice of automatically casting votes with proxy advisors' recommendations. Only two firms, including a witness who is on this panel today, are part of a duopoly, if you will, who are casting 97 percent of the proxy advisor market. They have given unprecedented power and control over my constituents' 401(k)s and their future funding.

Essentially, for a corn grower who lives in my home State, their livelihood to both fuel and feed the world is being unknowingly funding groups who are committed to demising their very line of existence, their hard-earned 401(k) portfolio investment and advisors, who are voting on their shares, both solely on the recommendations of these two firms that operate oftentimes in opposition to those very farmers, livestock producers, and biofuels upon which hey have built their businesses. In fact, in some cases, they are openly hostile competitors and overseas companies where their retirement dollars are going. This can impede and even seek to end traditional farming in my State, and that is just one sector.

In Iowa, growers who are also investors have little knowledge and only two respectable options to choose from in terms of proxy advisors. Not only are farmers losing funds to their competition, but they are losing market performance on those hard-earned retirement funds. According to Forbes, numerous studies demonstrate and correlate between an increase in activism in areas like environmental activism, and to public pension funds promoting social agendas and lower stock returns, resulting in a staggering 14-percent decrease in valuations for those affected companies.

To that end, Madam Chairwoman, I am introducing a bill next week that requires the SEC to make a final rulemaking prohibiting the practice of robo-voting and prohibits institutional investors from outsourcing their voting decisions to a proxy advisor. It requires them to be based on investment merit returns versus activist desires. In my opinion, it is beyond time that this corrupt and largely lazy practice is brought into the light and ended. Our constituents are counting on us for this level of change.

With that, Mr. Netram, can you go into detail and describe to us the process of robo-voting and how it impacts the decision-making process and the fiduciary responsibilities of asset managers?

Mr. NETRAM. Absolutely. Thank you for that question, Congressman. Robo-voting, as you so accurately described it, is the process by which proxy firms automatically cast votes on asset managers' behalf in line with those proxy firms' recommendations and without any review by the asset managers. What you have is a system in which asset managers don't have the ability to make an informed decision on the votes that they are taking because the proxy firms are just automatically casting those votes. By definition, that means that those asset managers may or may not be acting in the Main Street investors' best interest.

Mr. NUNN. Why do you think then, that Chair Gensler of the SEC did away with former Chair Clayton's overhaul of proxy advisor firms in 2020? And do you think that a robo-voting bill, like the one I am proposing this morning, is a priority?

Mr. NETRAM. On the second question, absolutely. Thank you for leading on that legislation, Congressman. I think it is absolutely needed and a real priority for the industry. On the first question about Chairman Gensler's actions here, it is hard to know his mind, but it certainly does seem to be part and parcel of the SEC's overall effort to deregulate and empower proxy advisory firms. The net effect of this is that your constituents, Iowans, are left with conflicted, error-ridden advice that is being automatically voted on their behalf without them even knowing about it.

Mr. NUNN. Thank you, Mr. Netram. With that, Madam Chairwoman, I yield back.

Chairwoman WAGNER. The gentleman from Iowa yields back. The Chair now recognizes the gentlewoman from Indiana, Mrs. Houchin, for 5 minutes.

Mrs. HOUCHIN. Thank you, Chairwoman Wagner and Ranking Member Sherman, and thank you to each of the witnesses for your testimony and for speaking with us today. One of my top priorities as a member of this committee is to protect retail investors and ensure that my constituents in Southern Indiana are given the same

financial opportunities and the level of priority as investors in any other part of the country.

When I hear from people back home, a constant point of concern is for the security of their wallets, the ability to save for retirement, provide for their families, and secure their futures. As my colleagues have discussed, the current system has lost sight of these priorities. Our capital markets and the soundness of our financial system have long been among our greatest strengths, but as political agendas and unrelated social issues drive the focus elsewhere, everyday Americans are forced to bear the cost of diminished returns and lost financial security. As a member of both the ESG Working Group, and this committee, I am glad we are now turning our attention to this issue. There is no reason why the well-being of everyday investors should take a backseat to politics over other unrelated issues.

Mr. Netram, you submitted a comment letter to the SEC back on September 12, 2022, regarding their proposed amendments on Rule 14a-8. As you stated in your letter, these proposals, "will ultimately force companies and shareholders to consider proposals any time an activist demands, irrespective of whether the company has already taken steps to address the underlying issue or whether shareholders have already considered and rejected or are currently considering a similar proposal." Needless to say, that is very concerning. As the current system works, activists can persistently resubmit similar proposals year after year, despite being previously rejected by a majority of the shareholders. By moving forward with this proposal, the SEC would place the interests of activists even higher than the well-being of their investors.

Mr. Netram, do you think it is fair for companies to have to continuously invest resources in fighting activist proposals that clearly do not benefit the company and its shareholders, especially when the proposals have been rejected in previous years?

Mr. NETRAM. Absolutely not. When a broad majority of shareholders have rejected a proposal, it is absolutely unfair for companies to have to continually reassess and re-engage with the activists on those ideas.

Mrs. HOUCHIN. And are there ways that we can reform this process, the no-action process, so that we can prevent these duplicative problems?

Mr. NETRAM. I think Congress has a real role to play here in reining in the SEC and directing them on a path that is more in line with the interests of mainstream investors.

Mrs. HOUCHIN. That is certainly part of the reason why we are here today, to really consider what package of bills we may be moving forward to address some of these issues. I am pleased to be leading an initiative that will address the issue. My bill will nullify this burdensome and unnecessary SEC proposal from taking place, saving shareholders both time and money and ensuring that the interests of a small number of activists don't take priority over our everyday investors.

Mr. Netram, the SEC's required mandate includes protecting investors, facilitating capital formation, and promoting efficient markets. How does the dominance of social and policy issues in corporate annual meetings conflict with those objectives?

Mr. NETRAM. The SEC can fulfill its mission to protect investors and support capital formation by allowing companies to really focus on long-term value creation. That is where their focus needs to be. What the SEC has done instead is they have taken steps to ensure or really encourage activists to hijack the proxy ballot and divert time, resources, and attention from the underlying business in which Main Street is investing.

Mrs. HOUCHIN. And I would argue that, in and of itself, is a threat to the general bottom line and overall performance of those shares for their shareholders. I am grateful to each of you for coming here to speak today. As we continue this important work on the committee, I hope we can ensure that the well-being of investors remains the chief focus of our capital markets. Thank you, Madam Chairwoman. I yield back.

Chairwoman WAGNER. The gentlelady from Indiana yields back.

And seeing no other Member on the dais has a question, I would just like to thank our witnesses today for their testimony.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

This hearing is adjourned.

[Whereupon, at 12:18 p.m., the hearing was adjourned.]

A P P E N D I X

July 13, 2023

WRITTEN STATEMENT OF JONATHAN BERRY, MANAGING PARTNER, BOYDEN GRAY PLLC

"Reforming the Proxy Process to Safeguard Investor Interests"
Hearing Before Subcommittee on Capital Markets, House Committee on Financial Services
July 13, 2023
Rayburn House Office Building
Room 2128
10:00 AM

Good morning, Chairman Wagner, Ranking Member Sherman, and members of the committee. My name is Jonathan Berry, and I am the managing partner of the law and public policy strategy firm Boyden Gray PLLC, where I provide strategic counsel and litigate on issues in the emerging field of bureaucratic overlap in government, corporate America, and capital markets, especially in matters relating to environmental, social, and governance (ESG) issues. I was previously the Acting Assistant Secretary for Policy at the U.S Department of Labor during the Trump Administration. Thank you for inviting me to testify today on the important subject of how the proxy process can better safeguard investor interests.

I currently represent the National Center for Public Policy Research and other shareholder clients in litigation against the SEC regarding its shareholder proposal rule, Rule 14a-8. While my views on the subject of today's hearing are informed by my representation of clients in this and other matters, I do not appear here today on behalf of any client, and the views I present are my own.

Background

In concept, the proxy process is supposed to provide an effective means by which public company investors can represent their interests. The proxy process derives its name from the legal fact that the many financial intermediaries who compose it possess their powers to act "by proxy." That is, the asset managers and proxy advisers who make up the proxy system act *on behalf of* the Americans whose savings they (or their clients) manage in trust. Symbolically, the "proxy process" is supposed to replicate, in modern and virtual form, the traditional stockholder meeting that existed in early American capitalism, where Americans with real skin in the game would attend to corporate affairs and ensure their financial interests were well represented. While scholars still debate the extent to which this traditional model of corporate governance in English and American history was myth or reality, at least in the eyes of the law, this is the backdrop from which the proxy process emerged.

Today, the proxy process falls far short of this ideal. Enabled by intrusive regulations and an overly concentrated and captured financial sector, the proxy process has unfortunately become dominated by activists who use it instead to advance political, social, and environmental agendas that are often contrary to the interests of the very shareholders the process is meant to serve.

We would expect that a well-functioning proxy process would represent the views of investors. What are those views? Research confirms the intuitive fact that retail investors are primarily interested in securing returns on their investments. In a recent survey by Consumers' Research, 70% of retail investors indicated that the primary use of their investment income is to

save for retirement or supplement their income. [1] By contrast, only 3% and 2% indicated they sought to advance sustainability or social change, respectively.[2] A survey of 1,128 retail investors conducted by the National Opinion Research Center at the University of Chicago (an independent, non-partisan research institution) and the FINRA Investor Education Foundation similarly found that individual investors prioritize return on investment and other financial factors in their investment decision-making more than any other factor, and identify the environmental aspects of a potential investment as the least important consideration.[3] Reflecting this intuition, the law as well assumes a baseline that investors will seek financial interests, whether in Justice Marshall's classic definition of the "reasonable investor," or the securities laws' inclusion of "expectation of profit" as an element of a security.[4] Deeper still, the essential structure of corporate law that shareholders buy into when they invest in public companies vests discretion in companies' boards of directors to manage the corporation for the best *financial* interests of the corporation and its shareholders.[5]

For these reasons, a reasonable proxy process would fairly reflect the fact that retail investors are primarily interested in securing returns on their investments. Yet today, the interests the proxy process *actually* reflects are nearly the opposite. Today, "environmental and social" proposals consistently comprise a majority of all shareholder proposals submitted to companies each proxy season as a result of the proxy process.[6] And these proposals are sometimes backed and often supported by a proxy-process infrastructure that has become dominated by large firms that themselves have publicly committed to advance environmental and social goals with companies.

With this testimony, I would like to survey for the Committee a key aspect and cause of this misuse of the proxy process: shareholder proposals under the SEC's Rule 14a-8. While there are several important problems with the current proxy system that members of this committee have highlighted, I believe shareholder proposals under Rule 14a-8 provide an excellent starting point for comprehension because they demonstrate the pervasive and insidious problems with the process.

To briefly summarize: Politically motivated shareholder proposals are a main entry point by which activists and financial intermediary firms that have adopted ESG-focused approaches

---

[1] Comment of Consumers' Research on The Enhancement and Standardization of Climate-Related Disclosures for Investors, https://www.sec.gov/comments/s7-10-22/s71022-20132345-302910.pdf.
[2] *Id*.
[3] FINRA Investor Educ. Found. & Nat'l Op. Res. Ctr. at the U. of Chi., Mar. 2022 https://www.finrafoundation.org/sites/finrafoundation/files/Consumer-Insights-Money-and-Investing.pdf
[4] *See* SEC Commissioner Elad L. Roisman, *Can the SEC Make ESG Rules that are Sustainable?*, June 22, 2021, https://www.sec.gov/news/speech/can-the-sec-make-esg-rules-that-are-sustainable.
[5] *See, e.g.*, *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986); *Dodge v. Ford Motor Co.*, 170 N.W. 668, 684 (Mich. 1919) ("A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end.").
[6] *See infra* Part II.B.

influence public companies to adopt their agendas. First, under Rule 14a-8, the SEC compels companies to provide activists with a platform for their agendas by requiring that companies include certain shareholder proposals in the proxy statements they send to all shareholders. In so doing, the SEC has made public companies the battlegrounds for contentious and polarizing issues that are properly the jurisdiction of our political branches of government. Moreover, through layers of regulatory and sub-regulatory guidance and an opaque process of administrative review, the SEC has virtually ensured shareholder proposals that represent *pro*-ESG viewpoints will make it onto companies' proxy statements, while so-called "anti-ESG" proposals are regularly denied access to the same. This skews the range of shareholder perspectives represented on the corporate ballot to overrepresent pro-ESG perspectives in the eyes of both shareholders and, importantly, managements and boards of directors.

With this beachhead position on the corporate proxy ballot secured, the rest of the market actors in the proxy process—proxy advisory firms, asset managers, and others—are empowered to drive corporate decisions by advising and recommending to clients how they should vote, or voting directly themselves on these select issues. And for market actors that themselves have pro-ESG agendas and investment methodologies (or who are concerned with the "optics" of these issues), votes on pro-ESG shareholder proposals present an opportunity to engage with and influence companies to adopt ESG-oriented goals rather than focus their limited resources on actually delivering returns to the investors who have entrusted them with their own limited capital.

Because this process chronologically begins with Rule 14a-8, I will discuss the rule's history and highly questionable validity, its misuse by the SEC over decades, and how the proxy-process infrastructure today uses Rule 14a-8 shareholder proposals to advance agendas that are contrary to the financial interests of companies and their shareholders. I will conclude with a brief discussion of recently proposed solutions.

I. The History of Shareholder Proposals and Rule 14a-8

I would like to begin by discussing the history of the SEC's shareholder proposal rule, Exchange Act Rule 14a-8. Rule 14a-8 requires publicly traded companies to include certain shareholder-submitted proposals in their proxy solicitations made to shareholders. Once included, shareholders (or, for most shareholders, their financial intermediaries) thereby can vote on those proposals by returning their proxies and affect the outcome for whether the company's shareholders elect to adopt the proposal.

While Rule 14a-8 has been with us for a long time, it has a questionable history that has often gone under-examined by policymakers. With the benefit of hindsight, I think I can safely say that a review of the rule's history makes it appear predestined to cause some of the abuses that we see today.

A. Like corporations, shareholder proposals arise strictly under state law.

To best understand the history of Rule 14a-8, we must look to where the concept of shareholder proposals comes from. The right of a shareholder to submit a shareholder proposal comes from state corporate law. Almost universally, corporations are chartered under state law because, in our system, states possess the primary power to grant corporate privileges and there is no general federal corporation law. As the Supreme Court has recognized, "[c]orporations are creatures of state law."[7] Like these other fundamentals of corporate governance, shareholder proposals then too are originally creatures of state law.

Historically, state law focused on whether a given shareholder proposal was a "proper subject."[8] Under this rule, shareholders could only consider shareholder proposals that presented a "proper subject" for action by the corporation's shareholders. Whether a proposal was a proper subject for action by shareholders depended on the scope of shareholders' powers under state corporate law. For example, some states permitted shareholders to remove directors at will, or required the unanimous consent of shareholders "for the institution of certain broad[] corporate policies."[9] Shareholder proposals that related to these valid exercises of shareholder powers were proper subjects and could be presented by a shareholder at a meeting of the corporation's shareholders. By contrast, a shareholder proposal that exceeded the shareholders' powers to act was not a proper subject and could not be validly considered. For example, a study contemporary to the SEC's proposal of Rule 14a-8 reported that under state law, "if a board of directors has the right to initiate the reduction of capital and a stockholder writes in and states that he proposes to make a motion that the capital be reduced, it would seem that such a motion may properly be declared out of order."[10]

Rule 14a-8 did not invent the shareholder proposal. To the contrary, prior to Rule 14a-8 there existed—and still exists—a robust system of state corporate law with which to evaluate shareholder-proposed items of corporate business. Many states still use the "proper subject" requirement or something like it.[11]

---

[7] *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 479 (1977).
[8] *See* David C. Bayne, *The Basic Rationale of Proper Subject*, 34 U. DET. L. J. 575 (1957).
[9] *Id.* at 582.
[10] Arthur H. Dean, *Non-Compliance with Proxy Regulations Effect on Ability of Corporation to Hold Valid Meeting*, 24 CORNELL L. REV. 483, 516 (1939).
[11] *See, e.g.*, Mich. Comp. Laws § 450.2404; N.C. Gen. Stat. § 55-7-01; 8 Del. Code § 109 (reserving to shareholders the power to amend corporate bylaws "relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees"). Under modern state laws, as under the historical common law approach, a proposal is a proper subject for action by stockholders if it is within the scope or reach of the stockholders' power to adopt. *See CA, Inc. v. AFSCME Emps. Pension Plan*, 953 A.2d 227, 232 (Del. 2008). A proposal that does not properly relate to shareholders' powers cannot be validly considered. For example, shareholders do not have the power to adopt proposals that would cause the board of directors to breach its fiduciary duties. *See Paramount Commc'ns Inc. v. Time Inc.*, 1989 WL 79880, at *30 (Del. Ch. July 14, 1989),

(footnote continues on the following page)

While state corporate law for over a century governed shareholder proposals, in general state law envisioned that shareholder proposals were business that would be transacted in person at companies' annual meetings. Originally, shareholder meetings were quite different from what we see today. Prior to the advent of large, vertically integrated corporations and the trading of corporate shares in public capital markets, corporations had relatively few shareholders, and shareholder meetings were conducted mainly in person.[12] The shareholders were often local and were active investors in the corporation. Shareholder proposals were most frequently referred to as "resolutions," and they were usually items of business, like amendments to the corporation's bylaws, or transactions.[13] The ability for a shareholder to submit resolutions was not a distinct or independent capacity, but arose from the more general common-law right of shareholders to attend the corporation's annual meeting or special meetings of shareholders. Presence at these meetings carried the right to propose items of business, such as nominating candidates for the corporation's board of directors, but also presenting shareholder proposals.[14]

As the structure of the conventional business corporation evolved away from trusts or small businesses with few or highly concentrated and active shareholders to publicly traded companies with many dispersed and largely passive shareholders, state corporate law changed with it. For a company to conduct its necessary business at an annual meeting, the company needed to obtain a quorum of shareholder votes present. But with the number and geographic distance of shareholders growing precipitously, obtaining enough shareholders to attend the meeting in person to achieve a quorum was more difficult than before. Instead, state corporate law developed the ability of shareholders to "attend" the annual meeting by proxy—in other words, by submitting written instructions to the company as to how the shareholder wished to vote on the business matters the company planned to consider. "Proxies" were forms by which a shareholder authorizes another person—usually a representative of the corporation—to vote his or her shares at the annual meeting. And that, of course, is where we get the phrase "proxy process" from.

B. With Rule 14a-8, the New Deal-era SEC overtook state law's authority over shareholder proposals.

It was against this state-law background that the SEC adopted Rule 14a-8 (originally enumerated "Rule X-14a-7") in 1942 under the auspices of Section 14(a) of the Securities Exchange Act of 1934.

Section 14(a) of the Exchange Act prohibits anyone from "solicit[ing] any proxy" "in contravention of such rules and regulations as the Commission may prescribe as necessary or

---

aff'd, 571 A.2d 1140, (Del. 1990) ("The corporation law does not operate on the theory that directors, in exercising their powers to manage the firm, are obligated to follow the wishes of a majority of shares.").
[12] *See* ADOLF BERLE & GARDINER MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 47–64, 139 (1933).
[13] *See* Jill E. Fisch, *From Legitimacy to Logic: Reconstructing Proxy Regulation*, 46 VAND. L. REV. 1129, 1136 (1993).
[14] *Id*.

appropriate in the public interest or for the protection of investors."[15] As the D.C. Circuit has interpreted, while the statute uses "broad[]" language, "it is not seriously disputed that Congress's central concern [in enacting § 14(a)] was with disclosure."[16] In enacting the Exchange Act, Congress expressly rejected a "federal corporation law" that would replace existing state law with a grant of authority to the SEC to regulate corporate governance.[17] Instead, Congress empowered the SEC to require that public companies disclose relevant information to investors. As the Senate report for the Exchange Act provides, the purpose of Section 14(a) was to ensure that investors had "adequate knowledge" about the "financial condition of the corporation . . . [and] the major questions of policy, which are decided at stockholders' meetings."[18] By contrast, while Section 14(a) gave the Commission authority to compel disclosures of existing information, Congress left the substantive regulation of stockholder meetings to the "firmly established" state-law jurisdiction over corporate governance.[19]

Though the language of Section 14(a) of the Exchange Act is a "vague 'public interest' standard . . . the Exchange Act cannot be understood to authorize the regulation of" "the substantive allocation of powers" in matters of "corporate governance traditionally left to the states."[20] The reach of its authority has a clear limit against state law. Section 14(a) does not authorize the Commission to impose upon matters of corporate governance traditionally governed by state law.

But that is precisely what Rule 14a-8 did. At first, the SEC treated its Section 14(a) authority, even as it related to shareholder proposals, as regarding disclosure. As recently as two years before finalizing Rule 14a-8, the SEC exercised its Section 14(a) authority to require that solicitation materials *disclose* "any matters which the persons making the solicitations are informed other persons intend to present for action at such meeting."[21] But just two years later, the SEC ratcheted its approach up further with Rule 14a-8. Purportedly exercising its authority under Section 14(a) of the Exchange Act to issue regulations for the public interest and the protection of investors, the SEC issued Rule 14a-8 in 1942. At the time the SEC proposed Rule 14a-8, state law did not require companies to include shareholder proposals in their proxy statements.[22] While under state law, shareholders possessed the right to present shareholder business at the corporation's annual meeting, state law did not require corporations to include shareholder proposals in their *own* proxy statements ahead of the meeting, sent to company shareholders. Instead, shareholders were free to solicit the proxies of other shareholders on their

---

[15] 15 U.S.C. § 78n(a)(1).
[16] *Bus. Roundtable v. SEC*, 905 F.2d 410 (D.C. Cir. 1990).
[17] See Stephen M. Bainbridge, *The Scope of the SEC's Authority Over Shareholder Voting Rights*, UCLA Res. Paper No. 07-16, https://www.sec.gov/comments/4-537/4537-17.pdf.
[18] S. Rep. No. 792, at 12 (1934).
[19] *Bus. Roundtable*, 905 F.2d at 411, 413 (internal citation omitted).
[20] *Id.* 407, 413 (internal citation omitted).
[21] SEC Release No. 2376, 1940 WL 7144 (Jan. 12, 1940).
[22] Susan W. Liebeler, *A Proposal to Rescind the Shareholder Proposal Rule*, 18 GA. L. REV. 425, 457–458 (1984).

own initiative in favor of a particular shareholder proposal they intended to present at the annual meeting. Rule 14a-8 upended this arrangement, first by compelling companies to include shareholder proposals, and over time by contorting the law governing the *substance* of shareholder proposals in ways far removed from shareholders' rights under state law.

C. Rule 14a-8 shareholder proposals have long provided social activists with a mechanism to influence companies.

From Rule 14a-8's earliest years, activists sought to use the rule to advance their political and social agendas at companies. While nowhere near the volume of shareholder proposals that companies face today, social activists ran a number of prominent issue campaigns at companies utilizing Rule 14a-8. "[S]ocial shareholder activism began as a tactic used by left-leaning social movements," from community organizing, to protests over napalm use in Vietnam, to Greyhound bus boycotts, anti-tobacco, and the "Make General Motors Responsible Campaign."[23] The left-wing activist Saul Alinsky even devoted an entire chapter of his book *Rules for Radicals* to organizing social movements to engineer change at large corporations. It was titled "Proxies for the People."[24]

When the rule was first adopted, Congress even anticipated that the rule would risk allowing shareholders to advance political agendas. In a 1943 hearing before the House Committee on Interstate and Foreign Commerce, Oklahoma Congressman Lyle Boren pressed SEC Chairman Ganson Purcell on whether a "Communist" activist could, "by the mere device of buying one share of stock" send a "propaganda statement" to "the mailing list of all the stockholders" of a company.[25] Congressman Boren could "see nothing [in Rule 14a-8] to prevent that statement from having some propaganda element in it," and Chairman Purcell agreed, saying that, assuming the Communist "otherwise complied with the rules, he could place a statement before all of the stockholders in the corporation."[26] To be sure, Chairman Purcell added that if a shareholder "were going to use the corporate proxy machinery for making a stump speech for some political party, that is obviously without the spirit of the rule," but addressing it might require that the SEC "make such appropriate changes as might seem necessary."[27]

Following from this concern, the SEC originally tried to close the floodgates of such social-agenda proposals that it had opened with Rule 14a-8. In a release published just three years after Rule 14a-8 was adopted, the SEC interpreted the rule to provide that "proposals which deal with general political, social or economic matters are not, within the meaning of the

---

[23] Leslie King & Elisabeth Gish, *Marketizing Social Change: Social Shareholder Activism and Responsible Investing*, 58 Sociological Perspectives 711, 714 (2015).
[24] Dan Willett, *Alinsky's Last Passion*, COUNTERPUNCH (Aug. 24, 2017), https://www.counterpunch.org/2017/08/24/alinskys-last-passion/.
[25] *H.R. 1493, H.R. 1821, and H.R. 2019, Hearing Before the H. Comm. on Interstate and Foreign Commerce* 163, 78th Cong. (1943), *available at* https://play.google.com/books/reader?id=7RaCMxk2dH8C&pg=GBS.PP4&hl=en
[26] *Id.*
[27] *Id.*

rule, proper subjects for action by security holders."[28] A subsequent version of Rule 14a-8 allowed companies to exclude proposals made "primarily for the purpose of promoting general economic, political, racial, religious, social or similar causes."[29] Nonetheless, shareholder activists continued to run campaigns on various issues and seek the inclusion of their proposals, building pressure for future rule changes.

II. The SEC's Blatant Viewpoint Discrimination Against So-Called "Anti-ESG" Proposals and Politically Conservative Shareholders

By implementing Rule 14a-8, the SEC compelled companies to include certain shareholder proposals in their proxy statements. Given the large number of shareholder proposals the rule invited, over the decades, the SEC developed a system of administrative review called the "no-action process" to review whether shareholder proposals complied with Rule 14a-8 such that they must be included in proxy statements. However, the process is highly opaque and unaccountable, and through it the SEC has come to privilege ESG-focused proposals' access to corporate proxies over other perspectives.

A. In the 1990s, the SEC developed the "significant social policy" exception and allowed social activists a path onto corporate proxy statements.

In 1976, the SEC amended the predecessor version of Rule 14a-8 discussed *supra* to remove its reference to the excludability of general economic, political, racial, and social causes.[30] At the same time, the SEC adopted what today is referred to as the "ordinary business" exclusion. In the same amendments, the SEC adopted the text of the ordinary business exclusion that remains essentially unchanged today: a proposal is excludable if it "deals with a matter relating to the conduct of the ordinary business operations of the issuer."[31]

At first, the SEC applied the ordinary business exclusion to permit the exclusion of proposals focusing on social issues. In 1992, in the landmark no-action response *Cracker Barrel Old Country Store, Inc.*, the SEC's Division of Corporation Finance stated its view that the exclusion allowed the company to block a proposal that requested the company "implement non-discriminatory policies relating to sexual orientation and to add explicit prohibitions against such discrimination to their corporate employment policy statement."[32] The Division noted that, in several previous cases, the Division had departed from the "general view that employment matters . . . are excludable as matters involving the conduct of day-to-day business" and made "exceptions" for certain "'social policy' concerns."[33] With *Cracker Barrel*, the Division clarified

---

[28] Op. of Baldwin B. Bane, Director, Division of Corporation Finance, Release No. 34-3638, 1945 WL 27415 (Jan. 3, 1945).
[29] *Amendments to Proxy Rules*, Release No. 34-4775, 1952 WL 5254 (Dec. 11, 1952).
[30] *Adoption of Amendments Relating to Proposals by Security Holders*, SEC, Release No. 12, 999, 1976 WL 160347, at *10 (Nov. 22, 1976); *see Trinity Wall St. v. Wal-Mart Stores, Inc.*, 792 F.3d 323, 338 (3d Cir. 2015) (tracing history of the ordinary business exclusion).
[31] 1976 Amendments, 1976 WL 160347, at *10.
[32] 1992 WL 289095, at *6 (Oct. 13, 1992).
[33] *Id*. at *1.

that under the ordinary business exclusion, a proposal's focus on a "social issue" did not "remov[e] the proposal from the realm of ordinary business operations."[34]

After *Cracker Barrel*, some SEC Commissioners and activist groups criticized the SEC's decision to allow companies to exclude social-issue proposals related to employment and pushed for changes in the SEC's interpretation of the ordinary business exclusion in order to permit greater proxy inclusion for social-issue proposals.[35] In a New York Times article titled *Equality Is More Than "Ordinary Business,"* Democrat Commissioner Steven Wallman called on the SEC to "remove any last barrier to getting employment nondiscrimination proposals back on the ballot."[36]

In 1998, the SEC responded to that pressure and reversed course. Noting "changing societal views" and that "the relative importance of *certain* social issues relating to employment matters has reemerged as a consistent topic of widespread public debate," the SEC reconsidered its approach adopted in *Cracker Barrel* by enacting the 1998 Amendments to Rule 14a-8. The SEC adopted changes to "reverse the *Cracker Barrel*" decision and narrow the ordinary business exclusion in order to prevent companies from excluding proposals that "focus[] on sufficiently significant social policy issues."[37] This became known as the "significant social policy" exception to the ordinary business exclusion.

B. Recent SEC guidance has opened the floodgates for a wave of social-activist proposals.

In the years following the adoption of the significant social policy exception, the number of shareholder proposals focusing on social and political issues have increased significantly. As the SEC recounted in a recent proposed rulemaking, from 2004 to 2018, proposals focusing on environmental issues grew from 5 percent to 16 percent of all shareholder proposals, and social-issue proposals from 25 percent to 39 percent.[38] Today, "shareholder proposals are now a central tool for shareholders seeking to advance social change."[39] Each proxy season, shareholder activists now submit hundreds of shareholder proposals on topics ranging from climate change to abortion and LGBT rights.

---

[34] *Id.*
[35] *See, e.g.*, *Proxies: SEC Should Reexamine Position on Shareholder Proposals, Wallman Says*, 28 Sec. Reg. L. Rep. (BNA) 1134 (Sept. 20, 1996); *Group Petitions SEC for Change on Proxy Resolutions about Employment*, 27 Sec. Reg. & L. Rep. (BNA) 1366 (Aug. 18, 1995) (petition of 30 institutional investors).
[36] Steven Wallman, *Equality Is More Than "Ordinary Business,"* N.Y. TIMES (Mar. 30, 1997), https://www.nytimes.com/1997/03/30/business/equality-is-more-than-ordinary-business.html.
[37] *Id.*
[38] Procedural Requirements and Resubmission Thresholds Under Exchange Act Rule 14a-8, 84 Fed. Reg. 66458, 66479 (Dec. 4, 2019).
[39] HEIDI WELSH, SUSTAINABLE INV. INST., & MICHAEL PASSOFF, PROXY IMPACT, 2023 PROXY PREVIEW 5 (noting "at least 542 shareholder proposals on environmental, social and related sustainable governance issues for the 2023 proxy season," which is "on track to match or exceed last year's unprecedented final total of 627").

In 2021, the SEC signaled it would allow even more social-issue proposals to be included in proxy materials. The Division issued Staff Legal Bulletin No. 14L ("SLB 14-L"), which explained even more forcefully that the significant social-policy exception does not "focus on . . . the nexus between a policy issue and the company, but will instead focus on the social policy significance of the issue that is the subject of the shareholder proposal," and thus turns on "whether the proposal raises issues with a broad societal impact, such that they transcend the ordinary business of the company."[40] SLB-14L further re-emphasized the 1998 Amendments' direction that "[m]atters related to employment discrimination" are an example of proposals that "may rise to the level of transcending the company's ordinary business operations."[41] Since SLB-14L was adopted, pro-ESG proposals have skyrocketed. The number of environmental and social proposals now represent a majority of all shareholder proposals received by Russell 3000 companies, comprising 58% of proposals in 2022 compared to 51% in 2021.[42]

With the development of the significant social policy exception and SLB-14L, Rule 14a-8 has gone a significant step beyond even its prior excess, as it now actively distorts, on an ideological basis, the substantive topics that companies and the shareholders consider through the proxy process. By the SEC's own interpretation of its own overreaching rule, the SEC has arrogated to itself the authority to define and decide what constitutes a "significant social policy" in our country.

As I will discuss next, the SEC now uses the significant social policy exception to further abuse the Exchange Act's neutral "disclosure" purpose by tilting the playing field in favor of shareholder proposals with certain content—namely, left-wing content. Under the current interpretation of Rule 14a-8, proposals that focus on certain kinds of discrimination—like racial quotas—must be considered, while proposals that focus on the other kinds of socially significant discrimination may be excluded from corporate proxy statements. None of this has anything to do with the shareholder value interests that underlie our system of corporate and securities law.

C. At the same time, the SEC arbitrarily sifts out conservative, independent, and other so-called "anti-ESG" proposals.

There has always been a sense that the SEC has catered to political progressives when it comes to proxy proposals. But of late the politicization of the SEC's own conduct has taken on a new and troubling life. The principal proof for this agenda is the SEC's arbitrary discrimination against proposals that express viewpoints that are not aligned with the current ESG dogma.

Recognizing that the SEC's changes to Rule 14a-8 over the years have opened corporate America to political influence by ideologically motivated shareholders, several individual

---

[40] Division of Corporation Finance, *SLB-14L* (Nov. 3, 2021), https://www.sec.gov/corpfin/staff-legal-bulletin-14l-shareholder-proposals.
[41] *Id.* at n.5.
[42] Daniel Litowitz et al., *Trends in E&S Proposals in the 2022 Proxy Season*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Nov. 28, 2022), https://corpgov.law.harvard.edu/2022/11/28/trends-in-es-proposals-in-the-2022-proxy-season/.

activist and politically conservative nonprofits have recently begun to submit their own shareholder proposals under Rule 14a-8. One of these entities is the National Center for Public Policy Research (the "National Center"), which I currently represent in litigation against the SEC. The National Center bills itself as "the nation's leading program for confronting liberal shareholder activism," and it uses shareholder engagement "to create the incentives for corporations to stay focused on their missions" and oppose the "liberal shareholder activism" that "continue[s] to exert undue influence over corporate America."[43]

Some describe proposals submitted by the National Center (and other shareholders who seek to counter pro-ESG proposals' influence) as focusing on ideologically conservative political issues. But in general, when these shareholder activists raise issues like abortion or 2nd Amendment rights, they do so to highlight *companies' own* political activism on a particular side of these issues—which itself is often driven by the influence of politicized actors in the proxy process. Many of these "conservative" activists' proposals are old-fashioned, good-governance reinforcements of fiduciary duty. For example, one proposal submitted by a leading wealth management investor this year called on a company to conduct an "evaluation . . . on the risks created by Company business practices that prioritize non-pecuniary factors when it comes to establishing, rejecting, or failing to continue business relationships."[44] Nonetheless, several media commentators and opposing activists derisively refer to these proposals as "anti-ESG."[45]

While so-called "anti-ESG" proposals have risen, the SEC has blocked many of them from consideration on company proxy statements via its no-action process, by which it affords relief to companies who seek to exclude purportedly non-complaint Rule 14a-8 proposals. The Society for Corporate Governance observed in a recent comment submitted to the Commission that in the 2022 proxy season, the SEC granted no-action relief in 50 percent of the instances where relief was requested on "anti-ESG" proposals—like the National Center's—compared with 38 percent across all proposals. The gap further widened when considering only social/political proposals, where the SEC granted relief at a 50-percent rate for proposals from "anti-ESG" proponents, as compared with 31 percent across all social/political proposals and 24% of environmental proposals considered by the SEC. These rates suggest "uneven grants of no-action relief . . . along ideological lines."[46] A comprehensive study by Consumers' Research

---

[43] *Free Enterprise Project*, Nat'l Ctr. for Pub. Pol'y Res., https://nationalcenter.org/programs/free-enterprise-project/ (last accessed May 25, 2023).
[44] *MetLife, Inc.* (SEC No-Action Letter, Apr. 24, 2023) at 3, https://www.sec.gov/files/corpfin/no-action/14a-8/bahnsenmetlife042423-14a8.pdf.
[45] Emile Hallez, *Anti-ESG shareholder proposals rise sharply*, INV. NEWS (June 2, 2023), https://www.investmentnews.com/anti-esg-shareholder-proposals-rise-sharply-238306; *see also* Scott Shepard & Stefan Padfield, *The Pro-Fiduciary-Duty Movement Is Winning*, Nat'l Ctr. for Pub. Pol'y Res. (June 28, 2023), https://nationalcenter.org/ncppr/2023/06/28/scott-shepard-stefan-padfield-the-pro-fiduciary-duty-movement-is-winning/ ("Advocates for Environmental, Social and Governance (ESG) policies label opponents as "anti-ESG." But what we really are is pro-fiduciary-duty.").
[46] *See* Letter from C. Edward Allen, Vice President, Soc'y for Corp. Governance, to Vanessa A. Countryman, Secretary, SEC, Sept. 13, 2022, https://www.sec.gov/comments/s7-20-22/s72022-20142742-308679.pdf.

confirms the SEC's viewpoint bias. For the 2018 through the 2022 proxy seasons, the SEC granted no-action relief under the ordinary business exclusion on 46% of all requests for liberal-aligned proposals in which it was raised, but 72% of all conservative-aligned proposals.[47]

While these aggregate disparities suggest a trend, the proof of discrimination is evident in comparing the proposals themselves. To illustrate, the following are proposals made by the National Center that companies sought to exclude under the ordinary business exclusion and that tracked very similar liberal-aligned proposals for which the SEC had previously denied no-action relief. Yet the SEC *granted* no-action relief against every single one of the proposals in the left-hand column:

Conservative-Aligned Proposal SEC Determined Excludable	**Liberal-Aligned Proposal SEC Determined Non-Excludable**
Report on "the potential risks associated with omitting 'viewpoint' and 'ideology' from its written equal employment opportunity (EEO) policy."[48]	Report on "the potential risks associated with omitting 'sexual orientation' and 'gender identity' from its written equal employment opportunity (EEO) policy."[49]
Report describing "if and how the Company intends to reduce the risk associated with tracking, collecting, or shaping information regarding the processing of payments involving its cards and/or electronic payment system services for the sale and purchase of firearms."[50]	Report describing "if and how the company intends to reduce the risk associated with the processing of payments involving its cards and/or electronic payment system services for the sale and purchase of untraceable firearms, including 'Buy, Build, Shoot' firearm kits, components and/or accessories used to assemble privately made

[47] *Consumers' Research SEC No-Action Audit 2018–2022* (May 4, 2023), https://consumersresearch.org/secnoactionaudit. These figures include proposals withdrawn by the shareholder proponent prior to the SEC issuing a no-action decision. If withdrawn proposals were subtracted, the disparity in no-action rates between liberal and conservative proposals would be even higher given that more liberal proposals are withdrawn (ordinarily after company settlement) than conservative proposals.
[48] *The Kroger Co.*, 2023 WL 2060072 (SEC No-Action Letter, Apr. 12, 2023).
[49] *CorVel Corp.*, 2019 WL 1640021 (SEC No-Action Letter, June 5, 2019).
[50] *American Express Co.*, 2023 WL 2524429 (SEC No-Action Letter, Mar. 9, 2023).

	firearms known as 'Ghost Guns.'"[51]
Report on "prioritization of non-pecuniary factors when it comes to establishing, rejecting, or failing to continue network relationships on its [Company] platform." Supporting Statement notes the company "shutdown [a] conservative news network" "following a concerted campaign by liberal activists" who claimed the company was "consistently giving airtime to conspiracy and misinformation" such as "conservative conspiracy theories ... that the 2020 presidential election was stolen."[52]	Report on "human rights impacts of [Company] content management policies to address misinformation and disinformation across its platforms." Supporting Statement cites to policies designed to prevent "attempt[s] to interfere with elections or civic processes."[53]
Report "on the risks created by Company business practices that prioritize non-pecuniary factors when it comes to establishing, rejecting, or failing to continue client relationships." Supporting Statement notes "[d]ebanking customers based on political, religious, or any other opinion or characteristic other than pecuniary advantage places the Company at great reputational, financial, and legislative and related risk" and "violates the Company's fiduciary duty to its shareholders."[54]	Request that the "Board of Directors take steps necessary to amend our certificate of incorporation ... to become a public benefit corporation." Supporting Statement notes that the proposal would "balance [the] interests of shareholders [and] stakeholders ... allowing the corporation to protect communities, even when it reduces financial return to shareholders in the long run."[55]

[51] *Mastercard, Inc.*, 2022 WL 392206 (SEC No-Action Letter, Apr. 22, 2022).
[52] *AT&T Inc.*, 2023 WL 108213 (SEC No-Action Letter, Mar. 15, 2023).
[53] *Alphabet Inc. (W. Andrew Mims Trust)*, 2022 WL 392221 (SEC No-Action Letter, Apr. 12, 2022).
[54] *JPMorgan Chase & Co.* (SEC No-Action Letter, Mar. 21, 2023).
[55] *Alphabet Inc.*, 2021 WL 389302 (SEC No-Action Letter, Feb. 23, 2021).

Requesting that companies publish their "diversity, equity or related employee-training materials" after they "adopt 'anti-racism' programs" that "distribut[e] pay and authority on the basis of race ... rather than by merit."[56]	Requesting that the company publish a "publicly disclosed" audit analyzing its "impacts on civil rights, equity, diversity and inclusion."[57]

The National Center's litigation against the SEC centers on the first proposal in the above list, which relates to viewpoint discrimination in employment. The proposal sought to ensure transparent oversight by Kroger of the risks associated with failing to prevent discrimination against its employees on the basis of viewpoint or ideology.

The National Center modeled its Kroger proposal on an earlier proposal on an ESG issue that the SEC had previously said was *not* excludable because of the significant social policy exception. A 2019 proposal in *CorVel Corp.* requested that the company "issue a public report detailing the potential risks associated with omitting 'sexual orientation' and 'gender identity' from its written equal employment opportunity (EEO) policy."[58] The Division determined that the company could not exclude the proposal under the exception because it "transcend[ed] ordinary business."[59] This outcome was consistent with the Division's longstanding position, post-1998 Amendments, that proposals focusing on issues relating to employment discrimination on the basis of sexual orientation and gender identity are not excludable under the significant social policy exception.

The National Center's Kroger proposal was identical to the proposal in *CorVel Corp*, except it substituted "viewpoint" and "ideology" for "sexual orientation" and "gender identity." In its briefings before the SEC, the National Center cited extensive statistics about the existence of viewpoint and ideological discrimination in corporate America and at Kroger, as well as the social significance and public debate over that issue. The National Center argued that viewpoint discrimination, the rise of "woke" capital, and its effect of discriminating against Americans based on their political viewpoints are issues that concern millions of Americans and are among the most hotly debated subjects in politics today, comparable to the sexual-orientation discrimination issue raised by other proposals.

Why did the Division grant Kroger no-action relief while denying it to CorVel for a nearly identical proposal that focused on progressive concerns in employment discrimination? The SEC's pattern of disfavoring conservative proposals is the only rational explanation. Both

---

[56] *See, e.g.*, *Verizon Communications Inc.*, 2022 WL 110304 (Mar. 17, 2022).
[57] *Amazon.com, Inc. (N.Y. State Common Ret. Fund)* (SEC No-Action Letter, Apr. 7, 2021), https://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2021/nyscrfamazon040721-14a8.pdf.
[58] *CorVel Corp.*, 2019 WL 1640021 at *1 (SEC No-Action Letter, June 5, 2019).
[59] *Id*.

issues involved discrimination, which the SEC itself has said is the prototypical issue that transcends ordinary business operations, and both issues are the subject of intense public debate.

The National Center's litigation with the SEC provides a prime example of the SEC's discrimination, which ensures that pro-ESG viewpoints are overrepresented in the proxy process.

III. Rule 14a-8 Shareholder Proposals: The Raw Material of the ESG-Focused Proxy Machinery

The problems that Rule 14a-8 presents are not limited to viewpoint discrimination by the SEC against conservative and other so-called "anti-ESG" shareholder proposals. That is only the starting point. Once the SEC has deemed that a company must include a pro-ESG shareholder proposal on its proxy statement (and sometimes even before then), the rest of the proxy process takes over to use the proposal as an opportunity to influence companies to adopt ESG goals related to the proposal, regardless of whether those goals are in the economic interests of shareholders. To use a metaphor, the shareholder proposal is the raw material that the machinery of the proxy process converts into the finished product of corporate commitments to various environmental, social, and political goals.

A. Proxy advisers, asset managers, and other component actors in the proxy process use Rule 14a-8 shareholder proposals as leverage with companies to urge the adoption of ESG-oriented goals.

Shareholder proposals are one of the main entry points for ESG agenda items to make it onto *companies'* agendas. To paraphrase SEC Commissioner Hester Peirce, shareholder proposals "introduce new pressure points that activists—or stake-holders as some prefer to call them—can use to strong-arm uncooperative funds [and companies] into instituting policies more conducive to the activists' agendas or punish funds [and companies] that fail to fall in line."[60] I

To understand how this happens, I will first provide a brief overview of other actors in the proxy process, and then describe how those actors use Rule 14a-8 shareholder proposals to effect corporate commitments to their agendas.[61]

i. Key actors in the proxy process.

First, in addition to shareholder activists, there are a range of other non-shareholder activist entities who coordinate shareholder-proposal activism on social and environmental issues. For example, the group Climate Action 100+ coordinates the investment strategies of over 700 investors with over $68 trillion in assets toward the stated goal "to ensure the world's largest

---

[60] SEC Commissioner Hester Peirce, *Statement on Environmental, Social, and Governance Disclosures for Investment Advisers and Investment Companies*, May 25, 2022, https://www.sec.gov/news/statement/peirce-state-ment-esg-052522.

[61] The remainder of this section borrows heavily from the report published by Consumers' Research discussed *infra* note 78.

corporate greenhouse gas emitters take necessary action on climate change."[62] Notable investor signatories to the network include asset managers like BlackRock, State Street, Goldman Sachs, and J.P. Morgan Asset Management, as well as institutional investors like the California Public Employees' Retirement System ("CalPERS"), the California State Teachers Retirement System ("CalSTRS"), the New York State Common Retirement Fund and Teachers' Retirement Fund and the Harvard University Endowment.[63] Climate Action 100+ organizes its investors to engage with "focus companies" and "seek commitments on the initiative's key asks" of taking "action to reduce greenhouse gas emissions across the value chain."[64] If investors engage with companies on an individual basis, they "are required to share information with the engagement working group and the coordinating investor network" and "liaise with relevant network staff and/or lead investors to ensure engagement priorities and ambition are aligned with the goals of the initiative, as well as with the overall collaborative approach."[65] Other coordinating entities like Climate Action 100+ serve to organize shareholder proposal campaigns against targeted companies.

Second, proxy advisers, the largest of which are Institutional Shareholder Services ("ISS") and Glass Lewis, who control upward of 90 percent of the relevant market, advise many funds on how to vote on shareholder proposals. For example, ISS recommends voting against directors of companies "on the current Climate Action 100+ Focus List" unless the company has issued "[d]etailed disclosure[s] of [its] climate-related risks" and implemented "Net-Zero-by-2050 [green-house gas emissions] reduction targets."[66] Pursuant to that guideline, ISS recommends its clients vote in favor of shareholder proposals that would require companies set these goals. In 2021, Glass Lewis recommended voting in favor of shareholder proposals recommending "racial equity audits" at least seven companies.[67] The proxy voting recommendations of these proxy advisers, both of which are foreign-owned, are incredibly influential, driving vote outcomes and impacting the financial well-being of millions of retail investors each year, while effectively setting energy and social policy for the United States through corporate governance.

Third, the asset managers BlackRock, Vanguard, and State Street Global Advisors together manage over $20 trillion in assets and cast an average of 25 percent of the votes at S&P

---

[62] *About*, CLIMATE ACTION 100+, https://www.climateaction100.org/about/ (last accessed July 11, 2023).
[63] *Who is Involved, Investors*, CLIMATE ACTION 100+, https://www.climateaction100.org/whos-involved/investors/ (last accessed July 11, 2023).
[64] *Approach, How We Work*, CLIMATE ACTION 100+, https://www.climateaction100.org/approach/how-we-work/ (last accessed May 28, 2023).
[65] *Id.*
[66] Institutional S'holder Servs., *U.S. Proxy Voting Guidelines 2022*, ISS GOVERNANCE at 17 (Dec. 13, 2022).
[67] Ron S. Berenblat et al., *Racial Equity Audits: A New ESG Initiative*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Oct. 30, 2021), https://corpgov.law.harvard.edu/2021/10/30/racial-equity-audits-a-new-esg-initiative/.

500 companies.[68] These asset managers often engage in favor of pro-ESG priorities yet do not provide evidence that their votes or perspectives are in the best economic interest of the shareholders on behalf of whom they vote and engage. BlackRock's 2021 voting guidelines exhorted, for example, that "boards should aspire to 30% diversity of membership and encourage companies to have at least two directors on their board who identify as female and at least one who identifies as a member of an underrepresented group."[69] State Street similarly has adopted voting guidelines that would require boards to adopt race and sex-based quotas.[70] And on environmental issues, for instance, BlackRock voted against the re-election of the board chair at TransDigm, a U.S. aviation manufacturer, for failure to "to adopt quantitative greenhouse gas emissions goals."[71]

ii. How proxy-process market actors use shareholder proposals to influence companies to make ESG commitments.

Proxy-process market actors use shareholder proposals in a variety of ways as leverage with companies.

In its most prominent form of influence, a shareholder proposal that successfully makes it onto the corporate proxy ballot and earns a majority vote of shareholders is considered "adopted" and creates immense pressure for management to implement its aims. Contrary to claims that dismissing shareholder proposals as non-binding, "[e]very proposal carries the implied threat to directors that their failure to respond to that proposal in the desired fashion will result in a coordinated effort to have those directors removed."[72] Both ISS and Glass Lewis caution in their voting guidelines that they will strongly consider voting against directors at companies that fail to respond to shareholder proposals that receive broad shareholder support.[73] As a result,

---

[68] *See* Lucian Bebchuk & Scott Hirst, *The Specter of the Giant Three*, 99 B.U. L. REV. 721, 736 (2019); Shaun Bisman & Felipe Cambeiro, *Big Three Institutional Investor Updates*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Apr. 13, 2022), https://corpgov.law.harvard.edu/2022/04/13/.

[69] BlackRock Inv. Stewardship, *Proxy voting guidelines for U.S. securities*, BLACKROCK (Jan. 2021).

[70] State Street, Guidance on Diversity Disclosures and Practices, at 2–3 (Jan. 2022), https://www.ssga.com/library-content/pdfs/asset-stewardship/racial-diversity-guidance-article.pdf.

[71] BlackRock Inv. Stewardship, *Our Approach to Sustainability*, BLACKROCK at 11 (2020), https://www.blackrock.com/corporate/literature/publication/our-commitment-to-sustainability-full-report.pdf.

[72] Letter from Austin Knudsen, Attorney General of Montana and 20 other state attorneys general, to BlackRock, JPMorgan, Goldman Saches, and 50 other asset managers (Mar. 30, 2023), https://attorneygeneral.utah.gov/wp-content/uploads/2023/03/2023-03-30-Asset-Manager-Letter-Press-FINAL.pdf.

[73] Glass Lewis, *2023 Policy Guidelines*, GLASS, LEWIS & CO. at 18 (2022), https://www.glasslewis.com/wp-content/uploads/2022/11/US-Voting-Guidelines-2023-GL.pdf?hsCtaTracking=45ff0e63-7af7-4e28-ba3c-7985d01e390a%7C74e0265a-20b3-478c-846b-69784730ccbd; *see* Institutional S'holder Servs., *United States Proxy Voting Guidelines 2022*, ISS Governance at 17 (Dec. 13, 2022), https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf?v=1 ("Directors should respond to investor input, such as that expressed through . . . significant support for shareholder proposals (whether binding or non-binding).").

shareholder proposals that receive a majority vote are often successful in securing company commitments.

Even shareholder proposals that fail to achieve majority support can also be influential. Glass Lewis's guidelines provide that companies' boards should be responsive to any shareholder proposal that achieves at least 20% of shareholder support contrary to the board's recommendation.[74] For example, JPMorgan Chase undertook a racial equity audit after 40% of JPMorgan Chase & Co. shareholders supported a so-called "racial equity" audit proposal submitted by the activist SOC Investment Group; in other words, the company determined to take this action after a clear majority of its shareholders voted against it.[75]

Shareholder proposals that do not receive significant shareholder support also provide pressure points for proxy-process actors to work with. In a 2020 comment, the pension fund and shareholder activist CalPERS called it "wholly inappropriate to measure [the] 'success' of a shareholder proposal by solely [sic] whether it was passed."[76] Instead, CalPERS described how "[s]hareholder proposals are a key component of our efforts to continuously engage with companies," and serve as a "tool[]" the fund uses to "engage in private discussions with management," "send letters" to corporate actors and stakeholders, and organize support for its agenda.[77] Shareholder proposals serve as platform for activists to communicate with one another and with other shareholders, and develop more successful campaigns down the road.

Votes on shareholder proposals position proxy-process actors like ISS, Glass Lewis, and large asset managers to ultimately play their trump card: denying reelection to corporate directors. These actors pressure companies through whipping up support for the actual shareholder proposals themselves, but those are formally precatory and non-binding. The real pressure comes in voting against or withholding votes from directors who fail to follow the activists' directions that are communicated via shareholder proposals. This forces individual directors to take a stand on those topics, or otherwise risk their careers.

An illustrative case study was documented in a recent report published by the group, Consumers' Research.[78] The case study highlights the background chain of events in the proxy process that concluded with the American oil and gas company Phillips 66 pledging to adopt "Scope 3" emissions-reduction targets in 2022. In the 2014 and 2015 proxy seasons, Phillips 66

---

[74] Glass Lewis, *supra*.
[75] JPMorgan Chase & Co., Submission of Matters to a Vote of Security Holders (Form 8-K), May. 18, 2021, https://www.sec.gov/ix?doc=/Archives/edgar/data/19617/000001961721000343/jpm-20210518.htm.
[76] Letter from Marcie Frost, Chief Executive Officer, CalPERS to Vanessa Countryman, Secretary, U.S. Securities and Exchange Commission 4 (Feb. 3, 2020), https://www.calpers.ca.gov/docs/legislative-regulatory-letters/02-20-comment-sec-shareholder-proposals.pdf.
[77] *Id.* at 3.
[78] *Defeating the ESG Attack on the American Free Enterprise System*, CONSUMERS' RES. (Mar. 8, 2023), https://consumersresearch.org/wp-content/uploads/2023/05/CR_Defeating-the-ESG-White-Paper_Final.pdf.

received shareholder proposals from activists that called on the company to disclose its carbon emissions and set reduction targets.[79] The 2014 proposal earned only 22% of shareholder support, and the 2015 proposal earned only 23%.[80] Of note, BlackRock voted against both proposals.[81]

While this activism at Phillips 66 was beginning, shareholder proposals were helping to influence other market actors in the proxy process, which would eventually help activists gain leverage over Phillips 66 and other energy companies. In the 2020 proxy season, the activist As You Sow submitted a shareholder proposal to BlackRock requesting a report on how the company intended to implement the Business Roundtable's 2019 Statement of Purpose to make the company "accountable to stakeholders" and "move[] away from shareholder primacy" in order to better "manage environmental, social, and governance matters."[82] While the proposal failed, soon after it was filed, BlackRock CEO Larry Fink publicly committed BlackRock to "plac[ing] sustainability at the center of our investment approach."[83] In response, the activists Boston Trust Walden and Mercy Investments publicly announced they had agreed to withdraw shareholder proposals on BlackRock's proxy statement in exchange for BlackRock's commitment to a "more active voting position" in companies in which BlackRock holds shares *on behalf of other investors* and on the basis of a "slew of new pledges on climate change and sustainability" by BlackRock.[84]

Back at Phillips 66, in May 2020 As You Sow (which is also a Climate Action 100+ signatory), submitted a shareholder proposal calling on Philipps 66 to report on the health risks

---

[79] Phillips 66, Definitive Proxy Statement (Schedule 14A), Mar. 26, 2014 at 70, https://www.sec.gov/Archives/edgar/data/1534701/000119312514115477/d663078ddef14a.htm#toc663078_24; Phillips 66, Definitive Proxy Statement (Schedule 14A), Mar. 25, 2015 at 60, https://www.sec.gov/Archives/edgar/data/1534701/000104746915002683/a2223551zdef14a.htm#Proposal_5.

[80] Phillips 66, Submission of Matters to a Vote of Security Holders (Form 8-K), May 7, 2014, https://www.sec.gov/Archives/edgar/data/1534701/000153470114000080/annualmeeting8-k.htm; Phillips 66 (Form 8-K), May 6, 2015, https://www.sec.gov/Archives/edgar/data/1534701/000153470115000052/psx8-k20150506annualmeetin.htm

[81] iShares, Inc., Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX), Aug. 27, 2014, https://www.sec.gov/Archives/edgar/data/930667/000119312514323161/d770504dnpx.txt; iShares, Inc., Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX), Aug. 26, 2015, https://www.sec.gov/Archives/edgar/data/930667/000119312515301938/d22371dnpx.txt.

[82] *BlackRock: Implementation Plan for New Business Roundtable "Purpose of a Corporation,"* AS YOU SOW (Dec. 12, 2019), https://www.asyousow.org/resolutions/2019/12/12/blackrock-corporate-purpose.

[83] Larry Fink, 2020 Letter to CEOs, *A Fundamental Reshaping of Finance*, BLACKROCK (2020), https://www.blackrock.com/corporate/investor-relations/2020-larry-fink-ceo-letter.

[84] Paul Verney, *BlackRock and JP Morgan spared ESG voting proposals following sustainability pushes*, Boston Trust Walden Co., RESPONSIBLE INV. (Mar. 10, 2020), https://www.bostontrustwalden.com/wp-content/uploads/2020/03/Blackrock-and-JP-Morgan-spared-ESG-voting-proposals-following-sustainability-pushes_.pdf.

of expanding petrochemical in areas "increasingly prone to climate-change induced storms, flooding, and sea level rise."[85] The Climate Action 100+ steering committee, which includes representatives of the Activists Ceres, CalPERS, and PRI, sent a letter to Phillips 66 requesting that the company commit to disclosures aligned with Climate Action 100+'s net-zero benchmark, and increased transparency of lobbying expenditures.

Finally, in the 2021 proxy season, Phillips 66 received a shareholder proposal from the activist Follow This calling for Scope 1, Scope 2, and Scope 3 reduction and targets and a CalSTRS and Presbyterian Church (U.S.A.) proposal calling for the company to produce a climate lobbying report. The emissions-reductions proposal was approved with 79% support, and the climate lobbying report with 62% support.[86] And this time, unlike at the start of the campaigns in 2014 and 2014, BlackRock flipped, supporting both proposals.[87] After Phillips 66 announced the results, Climate Action 100+ claimed victory:

> Following the 2021 annual meeting votes and further investor engagement around emissions reduction targets, later that year Phillips 66 became the first U.S. refiner and second U.S. oil company to set a Scope 3 emissions target, pledging a 15 percent reduction in emissions by 2030. . . . Investors will continue to engage closely with Phillips 66 to deliver on their commitments and set more ambitious targets for dealing with Scope 3 emissions, as well as increased alignment with the Climate Action 100+ Net-Zero Company Benchmark.[88]

This case study is but one of many examples of how the shareholder process plays a critical role in conducting influence operations on public companies.

B. Like the SEC, proxy-process market actors also arbitrarily discriminate in favor of ESG proposals.

Proxy advisers and asset managers have sometimes represented that they decline to weigh in on "political" shareholder proposals. But these claims are belied by the facts, which indicate that proxy advisers and asset managers are inconsistent with their treatment of political and ideological shareholder proposals.

---

[85] *Phillips 66: Report on Petrochemical Risks*, AS YOU SOW (2019), https://www.asyousow.org/resolutions/2019/12/10/phillips-66-report-on-petrochemical-risks.
[86] Phillips 66, Submission of Matters to a Vote of Security Holders (Form 8-K), May 12, 2021, https://www.sec.gov/ix?doc=/Archives/edgar/data/1534701/000153470121000116/psx-20210512.htm.
[87] iShares, Inc. Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX), Aug. 27, 2021, https://www.sec.gov/Archives/edgar/data/930667/000119312521258996/0001193125-21-258996-index.htm.
[88] *Phillips 66 increases Ambition of GHG Emissions Reduction Targets*, CLIMATE ACTION 100+ (Jan. 31, 2022), https://www.climateaction100.org/news/phillips-66-increases-ambition-of-ghg-emissions-reduction-targets-2/.

In a display of hypocrisy, asset managers will often recommend that their own shareholders vote against shareholder proposals proposed on their own proxy statements that the asset managers, in turn, vote in favor of at their portfolio companies. For example, Charles Schwab's board recommended that its shareholders vote against a shareholder proposal it received from the activist Friends Fiduciary Corporation to publish a detailed report of the company's lobbying activities.[89] Yet Charles Schwab voted in favor of substantially similar proposals to disclose lobbying activities to its portfolio companies Alphabet, Amazon, Eli Lilly, Netflix, Travelers, UPS, and Walmart.[90] Similarly, both Charles Schwab and State Street recommended against shareholder proposals requesting that the companies perform racial equity audits, but then voted in favor of racial equity audit-shareholder proposals at their own portfolio companies.[91] Following the trend, Northern Trust's board recommended its shareholders vote against a proposal that would require Northern Trust to prepare a report of its political contributions and expenditures. But Northern Trust's own investment arm voted in favor of proposals requiring Northern Trust (split vote), Western Union (split vote), and Fiserv to prepare reports of their political contributions and expenditures.[92] These examples make clear that these

---

[89] The Charles Schwab Corp., Definitive Proxy Statement (Schedule 14A), Apr. 1, 2022, at 92-95, https://www.sec.gov/Archives/edgar/data/316709/000119312522093320/d246025ddef14a.htm.
[90] Alphabet Inc., Definitive Proxy Statement (Schedule 14A), Apr. 22, 2022, at 70–73, https://www.sec.gov/Archives/edgar/data/1652044/000130817922000262/lgoog2022_def14a.htm; Amazon.com, Inc., Definitive Proxy Statement (Schedule 14A), Apr. 14, 2022, at 61–64, https://www.sec.gov/Archives/edgar/data/1018724/000110465922045572/tm223357-5_def14a.htm#tSHPR; Eli Lilly and Co., Definitive Proxy Statement (Schedule 14A), Mar. 18, 2022, at 72–75, https://www.sec.gov/Archives/edgar/data/59478/000005947822000099/lly def14a2022.htm#i9b9da9148a184c2c97520b2c3fd6d0c1_112; Netflix, Inc., Definitive Proxy Statement (Schedule 14A), Apr. 22, 2022, at 89–93, https://www.sec.gov/Archives/edgar/data/1065280/000119312522115102/d202881ddef14a.htm; The Travelers Companies, Inc., Definitive Proxy Statement (Schedule 14A), Apr. 8, 2022, at 68–71, https://www.sec.gov/Archives/edgar/data/86312/000008631222000019/a2022proxystatement.htm#ib65a69730f0f4e238d2897e7ecf4a773_1284; United Parcel Service, Inc., Definitive Proxy Statement (Schedule 14A), Mar. 21, 2022, at 62–64, https://www.sec.gov/Archives/edgar/data/1090727/000120677422000792/ups3995501-def14a.htm; Walmart Inc., Definitive Proxy Statement (Schedule 14A), Apr. 21, 2022, at 99, https://www.sec.gov/Archives/edgar/data/104169/000010416922000019/a2022proxystatement.htm.
[91] State Street Corp., Definitive Proxy Statement (Schedule 14A), Apr. 6, 2021, at 79–80, https://s201.q4cdn.com/681076340/files/doc_financials/2021/ar/STT-2021-Proxy-Statement.pdf; Amazon.com, Inc., Definitive Proxy Statement (Schedule 14A), Apr. 15, 2021, at 43–49, https://www.sec.gov/Archives/edgar/data/1018724/000110465921050333/tm2035374-1_def14a.htm. Oracle Corp., Definitive Proxy Statement (Schedule 14A), Sept. 24, 2021, at 78–81, https://www.sec.gov/Archives/edgar/data/1341439/000119312521282422/d162163ddef14a.htm.
[92] Northern Trust Corp., Definitive Proxy Statement (Schedule 14A), Mar. 12, 2019, at 65–66, https://www.sec.gov/Archives/edgar/data/73124/000119312519072131/d673202ddef14a.htm; The Western Union Company, Definitive Proxy Statement (Schedule 14A), Apr. 3, 2019, at 69–71, https://www.sec.gov/Archives/edgar/data/1365135/000120677419001208/wu3490101-def14a.htm; Fiserv

(footnote continues on the following page)

entities are missing the mark somewhere as it pertains to their fiduciary responsibilities—either to their own shareholders or to the shareholders of other companies on behalf of whom they are voting.

While I am working on further research to provide data on this front, proxy advisers and asset managers likewise will vote against "anti-ESG" proposals, even when they relate to the same subject matter as pro-ESG proposals, such as in employment discrimination. I am not aware of a single instance in which any of the largest and most significant proxy process actors have ever voted in favor of an "anti-ESG" proposal. By way of recent example, asset managers uniformly opposed the National Center's employee viewpoint discrimination proposal at Kroger, while simultaneously voting in favor of a "race and gender pay gap" proposal at Kroger, and also voting in favor of employee discrimination proposals at other companies on all sorts of liberal-focused subjects. In this way, the proxy process replicates in the private sector the same viewpoint discrimination against conservative viewpoints that the SEC does via government regulation.

IV. Overview of Recently Proposed Solutions

There are serious problems with the current proxy process, including with Rule 14a-8 and how market actors use it to advance unlawful objectives in corporate governance. Fortunately, there are several promising policy initiatives underway to try and solve or mitigate these issues, including those undertaken by this Committee.

A. Private ordering

While Rule 14a-8 purports to compel companies to include shareholder proposals that qualify under the rule's standards in their proxy statements, companies may be able to adopt their own internal corporate provisions to limit shareholder proxy proposals. Companies already regulate via corporate bylaws shareholders' ability to present proposal *in-person* at the annual meeting. While the conventional view is that Rule 14a-8 precludes companies from adopting bylaws restricting shareholder proposals that are inconsistent with Rule 14a-8,[93] the principal legal authority for this view, a Third Circuit opinion from 1947, is highly questionable.[94] Under state corporate law, companies are authorized to adopt, and many companies have in fact adopted, provisions in their charters that authorize the board of directors to unilaterally adopt bylaws, including bylaws relating to the rights of shareholders.[95] Once adopted, valid corporate bylaws are enforceable under state law. As I discussed *supra*, Rule 14a-8 is likely invalid to the

---

Inc., Definitive Proxy Statement (Schedule 14A), Apr. 9, 2019, at 69–70, https://www.sec.gov/Archives/edgar/data/798354/000119312519101679/d643515ddef14a.htm.

[93] *See generally* Stephen Bainbridge, *Can a corporation opt out of Rule 14a-8?*, PROFESSORBAINBRIDGE.COM (May 24, 2020), https://www.professorbainbridge.com/professorbainbridgecom/2020/05/can-a-corporation-opt-out-of-rule-14a-8.html (collecting sources from conflicting perspectives).

[94] *See Proxy Rule 14a-8: Omission of Shareholder Proposals*, 84 HARV. L. REV. 700, 704 (1971).

[95] *See, e.g.*, 8 Del. C. § 109(a), (b).

extent it intrudes upon state corporate law. If, pursuant to state corporate law, a company has validly altered the rights of its shareholders to submit shareholder proposals, I would consider it doubtful that Rule 14a-8 should operate to invalidate the company's lawful choice under state law.

Companies could take a range of approaches to stem the tide of unmeritorious shareholder proposals. SEC Commissioner Mark Uyeda thoughtfully explored these ideas in a recent speech delivered to the Society for Corporate Governance. In Commissioner Uyeda's view, "rule 14a-8's procedural bases for exclusion . . . should be viewed as default standards that apply only if companies decline to establish their own standards in their governing documents."[96] For example, a company could raise the minimum share ownership threshold required of shareholders to submit a proposal above the minimum $2,000 that Rule 14a-8 provides for. More substantively, a company could attempt to affirmatively exclude climate-related proposals, or other subject-matter areas.

While the possibility of greater private ordering would, in concept, allow for more diverse and efficient approaches to shareholder proposals, it is also no substitute for taking on other challenges in the proxy system. As the proxy process currently operates, issuers that adopt creative shareholder proposal-restricting bylaws would run the risk of running afoul of the market actors and the power they wield that I described *supra* Part III.A. That power must be highly restricted or broken up in order to allow for the market in corporate governance models to function properly.

B. Litigation challenging Rule 14a-8.

As I mentioned earlier, I currently represent the National Center for Public Policy Research in litigation against the SEC over the SEC's application of Rule 14a-8 to determine that the National Center's shareholder proposal focusing on viewpoint discrimination against companies' employees was not a "significant social policy." In that case, among First Amendment viewpoint-discrimination and other claims, the National Center argued in its briefings with the SEC that Rule 14a-8 exceeds the statutory authority of the Exchange Act.[97] The National Association for Manufacturers has intervened in the case and filed a brief arguing to similar effect.[98]

As Congress considers legislation modifying Rule 14a-8, it should consider ways to ensure that such changes do not affirm Rule 14a-8 and inadvertently deny meaningful judicial review to the SEC's unlawful conduct in issuing and applying it to private market actors.

---

[96] SEC Commissioner Mark Uyeda, *Remarks at the Society for Corporate Governance 2023 National Conference* (June 21, 2023), https://www.sec.gov/news/speech/uyeda-remarks-society-corporate-governance-conference-062123.
[97] The Kroger Co. (Apr. 12, 2023) at 26–28, https://www.sec.gov/files/corpfin/no-action/14a-8/nepprkroger041223-14a8.pdf.
[98] Nat'l Center for Public Pol'y Research v. SEC, No. 23-60230 (5th Cir., May 24, 2023), https://documents.nam.org/law/NAM_Intervention_Motion_NCPPR_v_SEC.pdf.

C. Legislation.

In conjunction with this hearing and related hearings, the Committee has presented several important bills that I believe would make valuable and important reforms to the proxy process. Each of the reforms to Rule 14a-8 proposed in the Committee's legislation under consideration would be a step forward in returning the proxy process to truly focus on investor interests. Specifically, I applaud the Committee for grasping the fundamental nature of the problems caused by Rule 14a-8 and proposing legislation to authorize the exclusion of shareholder proposals if the subject matter is environmental, social, or political—or, at least, eliminating the significant social policy exception—and, ultimately, prohibiting the SEC from continuing to implement Rule 14a-8.

I also commend the Committee's focus on ensuring proxy advisers and asset managers face greater accountability for how they recommend and vote on shareholder proposals. A private right of action against proxy advisers for advising that companies adopt shareholder proposals that violate state law, as Representative Steil's bill would do, would be a promising development. Creating binding voting rules for passive funds via the Investment Advisers Act, as one of the bills under consideration proposes, is an especially bold and innovative approach. Some ESG investing concepts flatly violate the Investment Advisers Act's provision of advisers' fiduciary duties to their clients,[99] but because enforcement discretion is left with the SEC, there has been little effort to police this misconduct. Inserting binding voting rules into the Advisers Act could be a valuable prophylactic measure for Congress to prescribe. Amendments to the Advisers Act would be a potentially powerful tool, and could be also be used to make clear there is no fiduciary obligation to vote all proxies, and that it is not a breach of fiduciary duty to vote in favor of all proxies supported by management.[100]

Finally, I would like to note that there is an increasing amount of legislative and regulatory activity going on in the states on these subjects. Numerous states have limited or prohibited the consideration of ESG investment methodologies with state funds. At the same time, Delaware, which is where the vast majority of public companies are incorporated and which has the most highly developed body of state corporate law, has increased liability risks for directors and management under the *Caremark* doctrine, which some have noted may supplement the SEC's recent pro-ESG disclosure proposed rulemakings and enforcement priorities.[101] If these trends continue, I anticipate that states will become increasingly creative in their efforts to either advance or defeat ESG concepts in corporate governance and asset management under state law. Forward-looking policymakers in Congress would do well to

---

[99] *See* Letter of Boyden Gray & Associates to Gary Gensler, Chairman, Securities and Exchange Commission 8–11 (Aug. 16, 2022), https://www.sec.gov/comments/s7-17-22/s71722-20137865-308198.pdf.

[100] SEC Commissioners Hester Peirce and Mark Uyeda, *Statement Regarding In the Matter of Toews Corporation*, Sept. 20, 2022, https://www.sec.gov/news/statement/peirce-uyeda-statement-toews-corporation.

[101] *See* Jacob H. Hupart et al., *Caremark Liability Following the SEC's New ESG Reporting Requirements*, Mintz (Dec. 16, 2022), https://www.mintz.com/insights-center/viewpoints/2301/2022-12-21-caremark-liability-following-secs-new-esg-reporting.

revisit federal securities and investment adviser statutes that preempt state law in these areas and attempt to identify solutions that allow for some constructive state-level experimentation.

I thank the Committee again for the invitation to testify today on this important subject, and I look forward to discussing it further with the Committee's members.

Bipartisan Policy Center
Where democracy gets to work

House Financial Services Subcommittee on Capital Markets
"Reforming the Proxy Process to Safeguard Investor Interests"

Good morning, Chairman Wagner, Ranking Member Sherman, and members of the subcommittee. Thank you for inviting me to testify today.

My name is Tim Doyle, and I am a senior advisor at the Bipartisan Policy Center, where I provide subject matter expertise on corporate governance and ESG-related matters. All opinions I express today are my own and do not necessarily reflect the views of the Bipartisan Policy Center.

The Bipartisan Policy Center (BPC) is a nonprofit organization founded in 2007 by four former Senate majority leaders—two Democrats and two Republicans: Howard Baker, Tom Daschle, Bob Dole, and George Mitchell. BPC drives principled and politically viable policy solutions through rigorous analysis, negotiation, and providing a forum for a diverse group of voices. BPC's funding reflects the character and diversity of the organization in that it comes from charitable philanthropies, individuals, and corporate donors. BPC believes that all its donors, as well as its project members, have unique and diverse interests. A strength of BPC's consensus-based negotiation process is that no single interest can unduly influence outcomes. However, we believe that bipartisanship is the only way to forge public policy solutions that are sustainable. And it is with that philosophy that I testify before you here today.

ESG in General

BPC has been evaluating and discussing ESG-related issues for a number of years and has come to realize that a growing number of people now know that the "E," in ESG focuses on environmental issues, that the "S," focuses on social issues, and that the "G" deals with corporate governance issues. However, we have also learned that the key to understanding ESG is looking at how one intends to use ESG-related data. As a result, the use of the ESG acronym varies widely depending on sector, company, and the individual person's perspective. This all-encompassing term has led some, on both sides of the political divide, to consider either breaking up the "E," "S," and "G" or coming up with a new term all together.

Given the difficulty in fully understanding the breadth of ESG-related topics, the committee should continue to work collaboratively with nonprofits, think-tanks, academics, and, of course, investors and corporations in finding common language when using the term "ESG." Furthermore, given the exponential growth in ESG investment funds and other financially based uses of the term ESG, establishing some consensus around the definition of ESG would greatly improve capital markets, further protect retail investors, and ultimately encourage more companies to go public.

Disclosure

At the center of the ESG debate is disclosure. Determining what is disclosed involves numerous factors

depending on if it is legislatively mandated, regulatorily required, or individually requested at annual shareholder meetings. My comments will focus on regulatorily required disclosure which has historically relied on issuers using a materiality analysis for determining disclosure, and the need for enhanced oversight of proxy advisors given the influence of their voting recommendations on ESG-related issues at annual shareholder meetings.

Materiality

I want to start by stating that BPC has been quite active in the ongoing development of the discussion around ESG-related issues over the past few years having submitted various comments to the SEC. These comments were largely based on numerous events we have held and input from our members.

Materiality, in particular, has been part of an ongoing discussion in BPC's Business Policy Project. BPC briefly addressed materiality in submitted comments[2] to the Securities and Exchange Commission ("SEC") in response to then-Acting SEC Chair Allison Herren Lee's 2021 request.[3] Then on July 20, 2021, BPC hosted an event to discuss "ESG disclosure and H.R.1187 with Representatives Congressmen Gregory Meeks (D-NY) and Bill Huizinga (R-MI).[4] We followed that event with one specifically on materiality on October 28, 2021 featuring two leading academic voices on the topic.[5] Then, after the release of the SEC's proposed "Climate Disclosure Rule," in March of 2022,[6] BPC hosted another event on April 7, 2022, discussing various aspects of the proposed rule including materiality.[6] BPC then submitted comments to the SEC on the proposed climate disclosure rule.[7] Then BPC hosted a fireside chat with Representative Huizenga in which materiality was again a topic of discussion.[8] Lastly, BPC hosted an event on April 13, 2023, to discuss the Department of Labor's rule on retirement savings wherein materiality was an integral part of the discussion.[9]

Background on Materiality (Reg. S-K. and ESG)

As this committee is well aware, the SEC is the lead regulatory agency for corporate disclosure. This falls under their tripartite mission to "protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation."[10] Over the years the SEC has created a framework of disclosure in furtherance of their mission. While most people understand the need for the disclosure of financial data for investors to make informed investment decisions, there has been growing interest in what has been referred to as non-financial data. ESG and other climate-related data have, until relatively recently, fallen under the category of non-financial.

The SEC has traditionally regulated non-financial data through Regulation S-K ("Reg. S-K"). Reg. S-K is the foundation of the existing framework for determining what non-financial information should be disclosed by issuers to the SEC.[11] Since its drafting in 1977, Reg. S-K has been updated numerous times as interest in various disclosure issues have developed.[12] Before the current proposed "climate disclosure rule," the SEC addressed what would be considered ESG-related disclosure issues, including climate-related risk, through its 2010 interpretive guidance ("2010 guidance") to Reg. S-K.[13] As a result, using a materiality analysis to

determine what to disclose under the 2010 guidance has been at the center of the disclosure debate for non-financial data.

Judicial Input

By the time Reg. S-K was finalized in the late 1970s, the issue of what type of information had to be disclosed had already been litigated numerous times and the SEC had already been using their own definition of materiality.[14] The seminal case involving the materiality standard was the 1976 Supreme Court case TSC Industries vs. Northway.[15] Justice Marshall's unanimous[16] opinion has probably been cited more often than any other case when discussing disclosure. The court held that a fact is "material," and thus should be disclosed, "if there is a substantial likelihood that a reasonable shareholder would consider it important …."[17] The court also held that when determining what to disclose "there must be a substantial likelihood that the disclosure … would have been viewed by [a] reasonable investor as having significantly altered the 'total mix' of information made available."[18] The SEC has recognized, cited, and used both the "substantial likelihood" and "total mix" language from the TSC Industry and its progeny of cases multiple times.[19] It is worth noting that the court acknowledged that applying a materiality standard could be difficult and stressed that materiality was "a mixed question of law and fact" and that it should only be found as a matter of law if "reasonable minds … [could not] differ on the question of materiality."[20] This last point is of particular importance given the attempt, in 2021, to pass a sense of Congress that ESG metrics are de facto material.[21] Given that the bill passed by one vote, it exemplifies that reasonable minds can and do differ on the parameters of material disclosure.[22]

Another area of concern, one in fact that the SEC expressed to the court, was the need to strike a balance between adequate disclosure on the one hand and having too low a standard for disclosure on the other.[23] In agreeing with the SEC at the time, the court found that "some information is of such dubious significance that insistence on its disclosure may accomplish more harm than good"[24]

Materiality Considered

The SEC is currently not obligated to include a materiality requirement to its proposed disclosures, though it is required to give a rational basis for its disclosure rules. Furthermore, while the SEC has no specific authority to require disclosure because it is material, companies are also under no obligation to disclose something unless there is a duty to disclose. As a result, historically, materiality has been used to bridge the gap between broad statutory language and specific disclosure requirements.

Mandating a materiality standard for disclosure would allow the SEC to address new disclosure issues without over burdening companies with disclosing endless amounts of information that any given investor finds relevant, and the potential of overwhelming investors by what the court described as an "avalanche" of data.[25]

In addition, adding a materiality standard could help insulate new disclosure requirements from litigation

claiming a proposed disclosure requirement does not promote efficiency, competition, and capital formation and therefore may be considered "arbitrary and capricious."[26]

While mandating a materiality standard for disclosure may be too simplistic of a solution for some, given the complexity of corporate disclosure and how and when materiality is applied, it can't be ignored that this standard has withstood the test of time for over 40 years. In writing the TSC Industries vs. Northway opinion, Justice Marshall seemed to understand the parameters of such a simple rule, but he also understood there would be "close calls." Important for contemplating legislative action is that the Court acknowledged that "doubts as to the critical nature of information misstated or omitted [would] be commonplace"[27] and the decision should favor disclosure in such cases as the securities laws are meant to "protect investors."[28] However, the court also explained that the deference to disclosure is based in part on the fact that issuers would presumably have "control" of the information to be disclosed.[29]

Other Organizations That Support a Materiality Analysis

It is also worth mentioning that the benefits of using materiality have been recognized by other organizations. For example, the SEC's Investor Advisory Committee recommended that "the Commission take action to ensure investors have the material, comparable, consistent information about climate and other ESG matters that they need to make investment and voting decisions".[30] The SEC has modeled their proposed Climate Disclosure Rule on the recommendations from the Task Force on Climate-Related Financial Disclosures (TCFD).[31] Specifically noteworthy is that the TCFD's disclosure framework was based on the evaluation of "material climate-related risks and opportunities".[32] The International Sustainability Standards Board's (ISSB) proposed standards require companies to "provide all material information related to significant sustainability matters that are relevant to investors' decision-making, including thematic and industry-based requirements."[33] The importance of materiality was also reinforced by the Value Reporting Foundation's May 6, 2023, comments to the SEC.[34] While TCFD, VRF, and the ISSB, have a broader definition of materiality than traditionally used by the SEC, they all nonetheless expressed the importance of a materiality qualifier as part of their disclosure frameworks.[35]

Conclusion for Materiality

Materiality is at the center of the disclosure debate. While keeping in mind that both the SEC's tripartite mission and congressional intent has been to create the world's most robust capital markets, protect investors, and maintain fair, orderly, and efficient markets, this committee should consider codifying the Supreme Court's, and historically the SEC's, standard for disclosure. Doing so would improve regulatory certainty for both investors and issuers.

Proxy Advisors

The transition in retirement systems from defined benefit to defined contribution may have been the single most influential factor in the exponential growth of institutional investors over the last couple of decades.[36] As their assets under management and corresponding ownership in publicly traded companies

increased, 70% by some estimates,[37] their responsibility to address shareholder rights on behalf of beneficial owners has also grown. This growth created a need to analyze and submit proxy votes at thousands of shareholder meetings each year. For example, in 2019, institutional investor Vanguard voted on over 169,000 proposals.[38] The New York City comptroller's office cast 71,000 ballots at 7,000 shareholder meetings in the first six months of 2018.[39] The sheer number of ballots that are reviewed and voted on has led to the growth of proxy advisory firms whose function is to review shareholder proposals and provide voting recommendations.

There are two firms, Institutional Shareholder Services (ISS) and Glass Lewis, that make up almost 97% of the market. However, concerns have been raised about the influence these firms have over voting results. As a result, questions have been raised about their recommendations and whether there should be more oversight and transparency around the proxy process and their recommendations to investors.[40] Specifically, concerns regarding conflicts of interest including how their recommendations are developed, erroneous reports supporting their recommendations, and the practice of what has been termed "robo-voting."

One of the issues that led to the concern about proxy advisory influence was that ISS and Glass Lewis appeared to offer similar vote recommendations for the same type of non-financial issues. As a result, there was a realization that their recommendations could have a significant effect on voting results. This impact was amplified by the growth of institutional investors.[41] Studies have shown that proxy advisor recommendations can have a significant impact on any given vote.[42] This includes both a direct impact on the vote tally and an indirect influence on corporate managers in how they attempt to avoid a negative recommendation.[43]

To complicate matters, investors and advocacy organizations have become more active in using corporate governance structures, such as proxy voting, to affect business decisions on issues ranging from environmental protection to human rights. This trend, which shows no sign of abating, begs the broader question of the extent to which the private sector should engage on public policy issues, and more specifically whether the current corporate governance structure was designed to facilitate these activities.

For over a decade there has been a bipartisan effort to implement additional oversight of proxy advisors and the proxy process more generally. I will focus on three concerns regarding proxy advisors including: 1) transparency of recommendations and conflicts of interest; 2) accuracy issues with the data used to make recommendations; and 3) the effect inaccuracies have when multiplied by robo-voting. Other issues such as, duties of financial advisors, resubmissions thresholds, vote tabulations, rights of beneficial owners, and liability have also been considered as part of reforming the proxy process.

While there are certainly arguments that could be made for the status quo given the need for proxy advisory services, given the changing dynamics of the proxy process Congress should consider robust

oversight of the proxy process.

Conflicts of Interest

There are two types of conflicts of interest with proxy advisors, one of which is unique to ISS. Specifically, ISS offers recommendations on proposals that are submitted for a vote by the same issuers to whom they offer consulting services on how to change or obtain favorable recommendations. ISS has explained that they have developed a process for addressing these types of conflicts by creating a "firewall" to insulate the different business lines based on guidelines used to determine the extent of the conflict. While actual conflicts are not publicly revealed, if one exists, clients are notified. ISS claims that any attempt to require them to disclose actual conflicts will weaken or destroy the firewall they are required to maintain.[44] However, proponents of proxy advisor reform have indicated that revealing guidelines to the assessment process used to determine conflicts of interest is insufficient to alleviate the appearance of impropriety.

The second potential conflict of interest is that some of the proxy advisors provide analyses to the same entities that regularly *submit* shareholder proposals. ISS claims that it has a set of policies that prevent conflicts from inappropriately affecting their decisions and that they notify clients of conflicts when they arise.[45] Others have argued that there is little to no oversight to ensure that the policies and procedures referenced are in fact followed.[46] The issue appears not to be about whether there are conflicts, as they do occur, rather whether there are sufficient procedures in place to address the conflicts when they occur.

Congress should continue their oversight and look for ways to ensure that the policies and procedures used to mitigate the potential conflicts of interest are effective, and that the recommendations made are transparent enough to protect investors and enhance our capital markets.

Errors in Reports

As with the conflicts of interest, there are also differing views on the amount of errors proxy advisory firms commit in their analyses and therefore, what effect, if any, they have on shareholder decisions. ISS indicates that they track errors in their reports and found that the error rate is less than 1%.[47] Moreover, a significant portion of the errors are not "errors" but rather differences of opinion over subjective analysis and methodology. ISS claims to engage year-round with S&P 500 companies and gives draft reports to some issuers 20 days in advance.[48] ISS also gives their clients alerts, through their Proxy Alert platform, about relevant errors in their reports. However, the U.S. Chamber has indicated that 3,700 public companies do not have the ability to interact with ISS regarding errors.[49] The chamber also argues the error rate is likely closer to 2.5% at a minimum, given that not all issuers file subsequent reports with the SEC documenting the errors.[50] In addition, the number of issuers that are requesting meetings with proxy advisors has declined noticeably, even though the error rate has not.

There is clearly a disagreement on the actual numbers and types of errors.[51] However, when tens of thousands of proposals are voted on every year, even a small percentage of errors could have a profound

effect on the information that is used to cast votes.

Given the direct and indirect influence that proxy advisor recommendations can have and the fact that successive administrations have disagreed on how that influence should be addressed regulatorily, Congress should develop a way for issuers to be able to review and correct errors in proxy advisors' reports so that investors have accurate information in which to make voting decisions. If there is a disagreement about the error, an investor should be able to know what the disagreement is based on. Lastly, engagement with proxy advisor error should not be correlated to a company's market capitalization.

Automatic and Robo-Voting

Automatic voting occurs when a proxy vote is based on a client's predetermined criteria to vote on certain issues. Robo-voting is the process by which voting occurs seemingly in response to the release of a proxy advisor's recommendation. While some of the largest institutional investors expend significant resources to evaluate both management and shareholder proposals, there is a concern that not all asset managers conduct proper oversight of their proxy voting decisions and instead outsource that analysis to proxy advisors.

Proxy advisors regularly assert that their recommendations are only intended to be a supplemental tool used in voting decisions. However, the data appears to show that a significant number of shares are "robo-voted" soon after a proxy advisor's recommendation. This concerning issue is amplified when recommendations are based on erroneous data coupled with the limited amount of time issuers are given to correct errors and the need for investment managers to align voting with fiduciary considerations.[52]

ISS claims that pre-populated ballots, associated with automatic voting, are based on custom reports, as opposed to their benchmark reports. Therefore, their clients have already predetermined how they will vote on many of the issues covered in the proposal process. Clients are the ones who determine what criteria they use to vote, and they have an annual review of the polices for their benchmark reports.

However, groups such as the U.S. Chamber argue that process is not sufficiently robust to address the magnitude of the problem. According to one report, up to 20% of voting occurs in substantial numbers within the three days of the release of a proxy advisor's report.[53] If there are substantial errors in the reports, votes would be based on inaccurate information, which in some cases could have profound effects on establishing the fiduciary duty asset managers owe to their clients. Moreover, with the use of pre-populated votes based on a predetermined set of criteria, there may be insufficient time to change one's vote if an erroneous report is relied upon.

While automatic voting with pre-populated votes saves investors time, the issue is whether there are sufficient safety mechanisms in place to "alert" investors of potential errors in reports before those votes are automatically submitted. Disabling the automatic function of submitting pre-populated votes, when

there has been an objection raised, certainly seems like it would help ensure that errors in reports and subsequent recommendations are not able to have a negative multiplier effect on the outcome of any given vote.

While there is circumstantial evidence that robo-voting occurs and in significant numbers to warrant review, the real question is whether there is a practical solution. Congress should contemplate possible practical solutions to this problem.

Conclusion on Proxy Advisor Reform

What has become apparent over the past two administrations is that the SEC's notice and comment process to provide a thoughtful regulatory framework to ensure certainty, has been turned into a political game of Ping-Pong. Given the vested interest in protecting investors and ensuring regulatory certainty, we may well have reached a point where Congress should consider taking action.

Therefore, to maintain a *transparent, accurate, and complete* proxy process, we want to reiterate the belief that issuers be given an opportunity to respond to inaccurate or arguably misinterpreted data. Most importantly that proxy advisors get this potentially updated data to their clients in a timely manner to make an informed investment decision. In addition to a proxy advisors' clients, one would hope that proxy advisory firms themselves would want to have the most accurate data before making voting decisions on behalf of their clients. Moreover, Congress should be concerned not just with whether a proxy advisor has accurate and complete information before disseminating their reports to the investors, but also the effect inaccurate and incomplete information can have on *all* investors.

Bipartisanship on Proxy Process

Proxy advisory reform, which had been contemplated by the SEC for more than a decade, has had bipartisan congressional support. This support goes back to at least the 114th Congress with the passage of H.R.5311[54] co-sponsored by Representatives John Carney (D-DE) and Sean Duffy (R-WI) with the support from eight other Democrats. In the 115th Congress, H.R.4015 was co-sponsored by Representatives Gregory Meeks (D-NY) and Duffy and passed the House with support from six Democrats.[55] After former SEC Chair Jay Clayton indicated his intent to promulgate rules on proxy advisors, Representatives Meek sand Duffy sent a joint letter asking the SEC to consider the concerns of transparency, accuracy, and conflicts of interest which were addressed in H.R.4015. After noteworthy changes to the SEC's 2020 proposal—as a result of input from proxy advisors, institutional investors, and academics—the final rule[56] was finalized along with additional guidance[57] in July of 2020. It was widely considered a compromise rule. It should be noted that ISS immediately filed a lawsuit and in November of 2021, current SEC Chair Gary Gensler proposed amendments to the 2020 rule. SEC Chair Gensler's amendments were adopted by the SEC on July 13, 2022, and went into effect September 19, 2022.[58]

While different administrations have taken slightly different approaches to these issues, one consistent

aspect has been a bipartisan desire to address the proxy process. There have also been several Republican and Democrat appointed SEC commissioners that have supported reforming the proxy process including additional oversight over proxy advisory firms.

- Former SEC Chair Mary Jo White (2013-2017) statement at the SEC 2013 roundtable that she was "particularly interested in the discussion of conflicts of interest that may or may not arise in connection with the participation of proxy advisers in our system."[59]
- Former SEC Chair Mary L. Schapiro (2009-2012) led the 2010 concept release which identified issues with proxy advisors.[60]
- Former SEC Commissioner Luis A. Aguilar (2008-2015) statement at the SEC 2013 roundtable indicating that the SEC "noted certain potential concerns relating to the activities of proxy advisors, including among other things the potential effects on shareholders of any conflicts of interest by the proxy advisory firm ... it is reasonable to ask if such actual or potential conflicts of interest can be effectively cured by disclosure and by efforts to insulate proxy advisory recommendations from a firm's consulting business."[61]
- Former SEC Commissioner Roel Campos (2002-2007) participated in a November 2019 BPC event indicating that "proxy advisors have a problematic business model"[62] with regards to their conflicts of interest.
- Former SEC Chair Elise Walter (2012-2013) participated in a February 2019 BPC event and signaled an openness to technical fixes regarding proxy advisors.[63]
- Former SEC Commissioner Joe Grundfest (1986-1990) indicated in a 2019 *Economist* article that he was supportive of giving issuers the opportunity to challenge the factual basis of recommendations.[64]

There has also been a long and distinguished list of bipartisan legislators who have supported proxy advisor reform over that past decade.

- In the 114th Congress, former Representative and now Governor John Carney co-sponsored H.R. 5311 the "Corporate Governance Reform and Transparency Act of 2016."[65]
- In the 115th Congress, Senator Jack Reed (D-RI) led the bipartisan Senate legislation with five cosponsors, including former Senators Heidi Heitkamp (D-ND) and Doug Jones (D-AL), on S.3614 the "Corporate Governance Fairness Act."[66]
- In the 116th Congress, 12 Democratic members of Congress, including Senators Krysten Sinema (D-AZ) and Senator Jackie Rosen (D-NV) who at the time was a member of the House, voted for H.R. 4015 the "Corporate Governance Reform and Transparency Act of 2017."[67]
- In addition, 10 Republican members of Congress cosponsored the "Corporate Governance Reform and Transparency Act of 2019" in support of reforming the proxy process.[68] Moreover, along with the 12 Democrats previously cited, 226 congressional Republicans supported H.R. 4015, the "Corporate

Bipartisan Policy Center
Where democracy gets to work

Governance Reform and Transparency Act of 2017[xviii] also dealing with reforming the proxy process and oversight of proxy advisors.

Conclusion

I truly appreciate the opportunity to share some of what we have learned over the last few years. BPC will continue to facilitate discussions and work to identify problems and bipartisan solutions in the capital markets. At BPC, we fully believe in the strength of bipartisanship to address issues that may otherwise get bogged down in the parochial politics of the day. BPC believes that even in the current hyper-partisan environment, bipartisanship can be found.

---

[1] BPC comments in response to then-Acting Chair Allison Herren Lee's, March 15, 2021 Statement "Public Input Welcomed on Climate Disclosure" (Jun. 11, 2021); *available at* https://www.sec.gov/comments/climate-disclosure/cll12-8911531-244352.pdf

[2] Then-Acting Chair Allison Herren Lee, Statement "Public Input Welcomed on Climate Disclosure" (Mar. 15, 2021); *available at* https://www.sec.gov/news/public-statement/lee-climate-change-disclosures

[3] BPC event "ESG Disclosure: A Conversation with Reps. Gregory Meeks and Bill Huizenga," (July 20, 2021) (Panel discussion with Hon. Gregory Meeks (D-NY) and Hon. Bill Huizenga (R-MI) to discuss ESG Disclosure and H.R.1187 the Corporate Governance and Improvement Protection Act of 2021), available at https://bipartisanpolicy.org/event/esg-disclosure-meeks-huizenga/

[4] BPC event "Do We Need to Rethink Materiality," (Oct. 28, 2021) (Panel discussion with Professors: Jill Fisch, University of Pennsylvania Carey Law School and Amanda Rose, Vanderbilt University Law School); *available at* https://bipartisanpolicy.org/event/do-we-need-to-rethink-materiality/ ; *see also* Timothy Doyle, BPC Blog "What is Materiality" (Oct. 27, 2021); *available at* https://bipartisanpolicy.org/explainer/what-is-materiality/

[5] SEC *Release* "The Enhancement and Standardization of Climate-Related Disclosures for Investors" (March 21, 2022, later conformed to the Federal Register versions) ("Proposal" or "Rule") at 9; *available at* https://www.sec.gov/rules/proposed/2022/33-11042.pdf; *see also* the proposed Rule (Apr. 11, 2022), 87 FR 21334; *available at* https://www.federalregister.gov/documents/2022/04/11/2022-06342/the-enhancement-and-standardization-of-climate-related-disclosures-for-investors

[6] BPC event "Corporations and Climate: Potential Impacts of the SEC's Proposed New Rule," (Apr. 7, 2022) (Discussion with former SEC Commissioner Troy Paredes); *available at* https://bipartisanpolicy.org/event/corporations-and-climate-potential-impacts-of-the-secs-proposed-new-rule/

[7] BPC submitted comments to the SEC regarding the proposed rule titled "The Enhancement and Standardization of Climate-Related Disclosures for Investors," (June 13, 2022); available at https://www.sec.gov/comments/s7-10-22/s71022-20131026-300399.pdf

[8] BPC event "Where Does the ESG Debate Go from Here?" (December 12, 2022) (Discussion with Hon. Bill Huizenga (R-MI), available at https://bipartisanpolicy.org/event/esg-debate/

[9] BPC event "What's ESG got to do with it? The impact of DOL's rule on retirement savings," (April 13, 2023) (Discussion with panelists Robert Eccles, Visiting Professor of Management Practice at the Said Business School, Oxford University; Anson Frericks, Co-Founder and President Strive Asset Management; Clara Miller, Advisor, Social Sector Finance; President Emerita Heron Foundation); available at https://bipartisanpolicy.org/event/dol-impact-on-retirement-savings/

[10] SEC, "About the SEC"; available at https://www.sec.gov/about

[11] *See* "Commission Guidance Regarding Disclosure Related to Climate Change," ("2010 Guidance") (Feb. 8, 2010), (Analysis of climate-related disclosure under Items 101 Description of Business; 103 Legal Proceedings; 105 Risk Factors; and revised 303 Management's Discussion & Analysis); *available at* https://www.sec.gov/rules/interp/2010/33-9106.pdf

Bipartisan Policy Center
Where democracy gets to work

[12] *See* "Adoption of Disclosure Regulation and Amendments of Disclosure Forms and Rules," Release No. 33-5893 (Dec. 23, 1977); 42 FR 65554 (Dec. 30, 1977).
[13] *See* 2010 Guidance at note 11 (Feb. 8, 2010); *available at* https://www.sec.gov/rules/interp/2010/33-9106.pdf
[14] *See* TSC Industry, Inc. v. Northway, Inc., 426 U.S. 438 (1976) ("TSC Industry").
[15] *Id.*
[16] Justice Stevens took no part in the case or decision.
[17] TSC Industry, *supra* note 14, at 449 (The holding applied to a decision on voting. The same rationale was used to extend its application to a decision to buy, sell, or hold a security in *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988).
[18] *Id.*
[19] Proposal, *supra* note 5, at 64 (Fn. 209 Citing 17 CFR 240.12b-2, under the Exchange Act, definitions "The term 'material,' when used to qualify a requirement for the furnishing of information as to any subject, limits the information required to those matters to which there is a substantial likelihood that a reasonable investor would attach importance in determining whether to buy or sell the securities registered."); *see also* 17 CFR 230.405 (Under the Securities Act, definitions "The term material, when used to qualify a requirement for the furnishing of information as to any subject, limits the information required to those matters to which there is a substantial likelihood that a reasonable investor would attach importance in determining whether to purchase the security registered"); *see also* Proposal at 166 (The Commission's discussion of applying the materiality standard to Scope 3 emissions).
[20] *See* TSC Industry, supra note 14, at 448.
[21] Corporate Governance Improvement and Investor Protection Act of 2021 (Jun. 16, 2021) (H.R.1187 was a large omnibus bill that had numerous disclosure provisions in over ten titles.); available at https://www.congress.gov/bill/117th-congress/house-bill/1187/actions
[22] Timothy M. Doyle, BPC Blog "'Disclosure Act' (H.R.1187): What it Means for the SEC and Other Stakeholders" (Aug. 25, 2021) ("The bill would have required the SEC to mandate disclosing information on political expenditures; pay ratios of certain employees; climate risk; tax havens; workforce demographics; workplace harassment; cyber security; board diversity; and forced labor. Proponents of the legislation argued investors need more ESG (including climate-related risk) information to make sound investment decisions. Opponents argued that under the existing regulations and materiality standard the types of information listed are already required to be disclosed if the information is material to a reasonable investor."); available at https://bipartisanpolicy.org/blog/disclosure-act/
[23] *Id* at 449 Fn. 10 (SEC filed an Amicus Brief with the U.S. Supreme Court).
[24] *Id* at 448-9.
[25] TSC Industry, supra note 14, at 449-450.
[26] 15 U.S.C. §78c(f) and §§78w(a)(2) and 80a– 2(c); see also Bus. Roundtable v. SEC, 647 F.3d 1144, 1148 (D.C. Cir. 2011); *see also* Am. Equity Inv. Life Ins. Co. v. SEC, 613 F.3d 166, 177 (D.C. Cir. 2010).
[27] *Id; see also* TSC Industry, *supra* note 14, at 448 (Citing Mills v. Electric Auto-Lite Co., 396 U. S. 375, 381 (1970).
[28] *Id.* TSC Industry at 448.
[29] *See id.* (This issue has become more important to the extent that any of the currently proposed SEC disclosure rules require disclosure of information not within the possession of the issuer.)
[30] Proposal, *supra* note 5, at 28-29.
[31] Proposal, *supra* note 5, at 37-39; *see also* TCFD' s final report and recommendations, p.14 (2017) (TCFD framework include eleven recommendations including four top level: Governance; Strategy; Risk Management; and Metrics & Targets); *available at* https://www.fsb-tcfd.org/wp-content/uploads/2017/06/FINAL-TCFD-Report-062817.pdf
[32] Proposal, *supra* note 5, at 39 (While TCFD's definition of materiality is broader than that which is used in the U.S. for SEC disclosure purposes, it is of note that there is a materiality analysis required in determining disclosure. One presumes that the SEC will be applying the U.S. definition in their disclosure framework.).
[33] ISSB FAQ, "How will the ISSB's standards approach materiality"; *available at* https://www.ifrs.org/groups/international-sustainability-standards-board/issb-frequently-asked-questions/
[34] *See* Janine Guillot, CEO Value Reporting Foundation (VRF) Comment on the

Bipartisan Policy Center
Where democracy gets to work

Enhancement and Standardization of Climate-Related Disclosures for Investors (May 6, 2022) (VRF, formerly SASB, will merge with ISSB in 2022); available at https://www.sec.gov/comments/s7-10-22/s71022-20127884-289400.pdf

[35] The VFR, at least when they referred to themselves as SASB, used a materiality standard based on the SEC's historic definition of materiality. However, the TCFD and presumably the ISSB look at materiality not only from how the human environment affects a company, but also how a company's action affects the human environment. This is typically referred to as "double" materiality.

[36] Dec. 27. 2021 CRS *In Focus* "A visual depiction of the shift from defined benefit to defined contribution pension plans in the private sector"; *available at* https://crsreports.congress.gov/product/pdf/IF/IF12007

[37] May 27, 2021, Paul Rose, Ohio State University College of Law, "Proxy Advisors and Market Power: A Review of Institutional Investor Robovoting," Harvard Law School Forum on Corporate Governance; available at https://corpgov.law.harvard.edu/2021/05/27/proxy-advisors-and-market-power-a-review-of-institutional-investor-robovoting/

[38] Vanguard Comments to the SEC's Roundtable on the Proxy Process" (Sept. 20, 2019); available at https://www.sec.gov/comments/4-725/4725-6168191-192387.pdf

[39] *Id.*

[40] BPC has hosted three public events as well as private roundtables on these important issues. We have been closely following the SEC actions on these matters since the November 2018 roundtable. On January 27, 2020, BPC hosted *The Proxy Process Reformed*, a discussion of proposed rule Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice. We had panelists Pat McGurn, Special Counsel and Head of Strategic Research and Analysis at Institutional Shareholder Services, Inc. (ISS) and Tom Quaadman, Executive Vice President at U.S. Chamber of Commerce Center for Capital Markets Competitiveness (U.S. Chamber).

[41] James R. Copland, David F. Lacker, and Brian Tayan, "Proxy Advisory Firms: Empirical Evidence and the Case for Reform," (May 2018); available at, https://media4.manhattan-institute.org/sites/default/files/R-JC-0518-v2.pdf

[42] *See* Id.

[43] *See* Id.

[44] BPC panel discussion on "The Proxy Process Reformed," with panelists Pat McGurn, Proxy Advisory ISS and Tom Quaadman, EVP U.S. Chamber (CCMC), moderated by BPC Sr. Advisor Timothy Doyle, *Bipartisan Policy Center* (January 27, 2020); available at https://bipartisanpolicy.org/event/the-proxy-process-reformed/

[45] *Id.*

[46] *Id.*

[47] *Id.*

[48] *Id.*

[49] *Id.*

[50] *See* Letter to the SEC from Ken Bertsch, Executive Director, Council of Institutional Investors (CII) ("we would expect that there are other undocumented errors"); available at: https://www.sec.gov/comments/4-725/4725-6357861-196392.pdf.

[51] On Jan. 27, 2020, BPC hosted "The Proxy Process Reformed," a discussion of the previously proposed Proxy Rules for Voting Advice. We had panelists from Institutional Shareholder Services, Inc. (ISS) and the U.S. Chamber

[52] Placenti, Frank M., "Are Proxy Advisors Really a Problem?" *American Council for Capital Formation (ACCF)* (October 29, 2018); available at https://accf.org/2018/10/29/are-proxy-advisors-really-a-problem/

[53] *Id.*

[54] H.R.5311 "Corporate Governance Reform and Transparency Act of 2016," (114th Congress 2015-16); available at https://www.congress.gov/bill/114th-congress/house-bill/5311/cosponsors?s=3&r=5&q=%7B%22search%22%3A%5B%22H.R.5311%2B114th%22%5D%7D

[55] H.R.4015 "Corporate Governance Reform and Transparency Act of 2017," 115th Congress 2017-18); available at https://www.congress.gov/bill/115th-congress/house-bill/4015?q=%7B%22search%22%3A%5B%22H.R.4015%22%5D%7D&s=5&r=8

[56] SEC "Exemptions from the Proxy Rules for Proxy Voting Advice" (*effective* Nov. 2, 2020); available at https://www.sec.gov/rules/final/2020/34-89372.pdf

Bipartisan Policy Center
Where democracy gets to work

[57] SEC "Supplement to Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers" (*effective* Sept. 3, 2020); available at https://www.sec.gov/rules/policy/2020/ia-5547.pdf
[58] SEC Press Release, "SEC Adopts Amendments to Proxy Rules Governing Proxy Voting Advice" (July 13, 2022); available at https://www.sec.gov/news/press-release/2022-120
[59] Chair Mary Jo White, "Welcoming Remarks at Proxy Advisory Services Roundtable" (Dec. 5, 2013); available at https://www.sec.gov/news/public-statement/open-meeting-statment-2013-12-06-mjw
[60] SEC's "Concept Release on the US Proxy System" (Release Nos. 34-62495; IA-3052; IC-29340; File No. S7-14-10) (2010); available at https://www.sec.gov/rules/concept/2010/34-62495.pdf
[61] SEC Commissioner Luis Aguilar Statement "Looking at Proxy Advisory Firms from the Investor's Perspective," (Dec. 5, 2013), available at https://www.sec.gov/news/public-statement/open-meeting-statement-2013-12-05-laa
[62] BPC's event "The Role of a Corporation: The Shareholder versus Stakeholder Debate" (Nov. 19, 2019); available at https://bipartisanpolicy.org/event/the-role-of-a-corporation-the-shareholder-versus-stakeholder-debate/
[63] BPC's event "Corporate Governance's Increasing Role in Public Policy: Opportunities and Limitations" (Feb. 7, 2019); available at https://bipartisanpolicy.org/event/corporate-governances-increasing-role-in-public-policyopportunities-and-limitations/
[64] The Economist, "Proxy advisers come under fire" (Nov. 14, 2019); available at https://www.economist.com/business/2019/11/14/proxy-advisers-come-under-fire
[65] H.R.5311, "Corporate Governance Reform and Transparency Act of 2016" (114th Congress, 2015-16); available at https://www.govtrack.us/congress/bills/114/hr5311/cosponsors
[66] S.3614, "Corporate Governance Fairness Act" (115th Congress, 2017-18) (Sens. Reed (D-RI); Perdue (R-GA); Heitkamp (D-ND); Tillis (R-NC); Jones (D-AL); and Kennedy R-LA); available at: https://www.congress.gov/bill/115th-congress/senate-bill/3614?q=%7B%22search%22%3A%5B%22Corporate+Governance+Fairness+Act%22%5D%7D&r=1
[67] H.R.4015, "Corporate Governance and Transparency Act of 2017" (115th Congress, 2017-18); (Members of Congress: Cooper (D-TN); Cuellar (D-TX); Delaney (D-MD); Foster (D-IL); Gottheimer D-NJ); Himes (D-CT); Meeks (D-NY); Peters (D-CA); Peterson (D-MN); *Rosen* (D-NV); *Sinema* (D-AZ); Suozzi (D-NY)); available at https://clerk.house.gov/Votes/2017702
[68] H.R.5116, "Corporate Governance Reform and Transparency Act of 2019" (116th Congress, 2019-20) (Members of Congress: Steil (R-WI); Wagner (R-MO); Riggleman (R-VA); Barr (R-KY); Gooden (R-TX); Budd (R-NC); Rose (R-TN); Timmons (R-SC); Hill (R-AZ); Hollingsworth (R-IN)); available at https://www.congress.gov/bill/116thcongress/house-bill/5116/cosponsors?r=2&s=1
[69] H.R. 4015, "Corporate Governance Reform and Transparency Act of 2017" (115th Congress)(Dec. 20, 2017); available at https://clerk.house.gov/Votes/2017702

Subcommittee on Capital Markets Hearing: "Reforming the Proxy Process to Safeguard Investor Interests"

July 13, 2023

Testimony of Nell Minow Vice-Chair, ValueEdge Advisors[1]

I am very grateful for the opportunity to share my thoughts on the proxy process and shareholder resolutions. I welcome your questions and will submit supplemental materials as necessary following this session and the related hearings on ESG and proxy advisors. I am particularly grateful for the opportunity to remind my fellow panelists about the essential elements of transparency and accountability that are the foundation of capitalism and the reason the markets of this country are the strongest, the most robust, and the greatest creators of wealth for investors and employees in the world. I am always disappointed to see the lengths corporate insiders and their service providers will go to insulate themselves from minimal transparency and feedback.

I have worked on behalf of shareholders since 1986 in a series of companies co-founded with Robert A.G. Monks and Rick Bennett, starting with Institutional Shareholder Services, all previous companies profitably sold and doing well. I met Bob Monks when I was at OMB and he was on the staff of then-Vice President George H.W. Bush on President Reagan's Task Force on Regulatory Relief, where we worked with the late Boyden Gray, who was an exemplar of free market economics.

I would like to state for the record that I have included my firm purely for identification. No one is paying me to be here and neither I nor our clients have any financial interest in any legislation or regulatory activity on these matters. I emphasize this because my experience with

[1] I have been following the issues we are here to comment on since 1986, when I was the fourth person hired and the first General Counsel of Institutional Shareholder Services. I met the founder of ISS, Robert A.G. Monks, when I was at OMB and he was working for then Vice President George H.W. Bush. We worked together, with the late Boyden Gray on President Reagan's Commission on Regulatory Relief. Later I was the CEO of ISS, until I left in 1990.

those who comment on these issues is that they often disguise their financial interest in the policies being discussed.[2]
The appendices to this testimony include my recent comment to OMB listing some of the Orwellian names of the fake, dark money front groups that are distorting the legislative and regulatory processes on these issues.

The sole and only reason capitalism works is the ability of investors, the providers of capital, to have some oversight to minimize what economists call agency costs and lawyers like me call conflicts of interest. We would not have capitalism if businesses took money from investors and just said, "Trust me." Markets do not run on money; they run on trust, and in the words of Ronald Reagan, "trust but verify." This is why the US has the most meaningful disclosure requirements in the world, but disclosure is not worth much if shareholders cannot respond to it.

That essential oversight is grounded in shareholder rights, including the ability to buy and sell, limited liability, shareholder litigation, and proxy voting, including votes on management proposals to elect directors, appoint auditors, and approve executive compensation, and advisory proposals from other shareholders on matters that fall within the very narrow requirements of the SEC's rules. For example, that means they cannot pertain to what is classified as "ordinary business," the daily decisions about products and operations. Yet they do have to be relevant, within the control of the company's board and managers. You can submit a shareholder resolution asking a software company to sell brownies, but the SEC will keep it off the proxy card. So the proposal has to be significant enough to be relevant but not central enough to constitute ordinary business. The proponent is limited to 500 words for discussion of the issue, while the company has no limits in its response and full access to the company treasury to fight it.

I am certain I do not need to explain to Members of Congress why it is important to allow affected parties to vote on important issues.

Four key points about shareholder proposals.

1. **Only a small percentage of companies receive proposals from shareholders each year.** The household name companies get several, and many companies get one or two, but most companies get none. The majority of public companies do not receive any shareholder proposals. On average, 13 percent of Russell 3000 companies received a shareholder proposal in a particular year between 2004 and 2017.2 In other words, the average Russell 3000 company can expect to receive a shareholder proposal once every 7.7 years. For companies that receive a shareholder proposal, the median number is one per year. Many of these proposals are withdrawn after conversations with the company. Self-reported, undocumented claims about the costs of reviewing and responding to shareholder proposals are wildly inflated and should be reviewed with skepticism as self-serving.
2. **Even a 100 percent vote in favor of a shareholder proposal is advisory only**[3]. Company executives can and do ignore significant, even majority votes. I am not

[2] For example: https://inequality.org/research/big-money-behind-fight-to-ban-responsible-investing/
[3] There is one small exception, but it is so rarely used, not once in recent memory, that it is not relevant here.

objecting to keeping shareholder proposals non-binding, which is in any event a matter of state law and outside the jurisdiction of Congress. But I emphasize that therefore, any downside risk from a shareholder vote on any topic is negligible, even non-existent. And the benefit of knowing what investors think is enormous; if management disagrees with the vote, at least they will learn that they are not communicating effectively and can do better. Limiting shareholder proposals is killing the messenger. It would be like telling customers they could not complain about products or services. Proposals are one of the very few ways insulated insiders hear honest feedback.

3. **While a small number of people are responsible for a large percentage of shareholder proposals, the far more significant number is the level of support those proposals receive**. We already have a system in place to keep proposals that do not get minimum levels of support off the proxy card, and indeed that was the fate of most of the anti-ESG proposals voted on this year. But it does not matter who files the proposals; what matters is whether they get widespread support from a variety of shareholders. If there are votes in favor from large and small funds and individuals, index funds and managed funds, pension funds and foundations, that is the best possible market test, and market tests are what keep companies and the economy strong.
4. **No one is required to purchase the services of a proxy advisory firm**. Many institutional investors do not. Those who do are not obligated to follow their recommendations. Indeed, the data show that while they do follow the advice on routine matters like re-electing directors and approving auditors (over 90 percent of proxy advisor recommendations are to vote with management), their clients review their analyses and then make their own decisions on the more complex and controversial issues like business combinations. ProxyInsight produced a study[4] proving that only 21 percent of investors use the proxy voting policy of a Proxy Voting Advisor and of the 1,086 investors surveyed 70.9 percent vote proxies based on their own policies with a further 8.5 percent delegating to a sub advisor or other asset manager.

   These services are purchased by the most sophisticated financial professionals in the world. Those that choose to work with a proxy advisor can pick a registered investment advisor, one that is a registered NRSRO, or one who is not, one that offers consulting services to corporations or one that does not. Or more than one, to compare their analyses, as some do. While there have been claims over the past few years that there is a "duopoly," that is clearly not the case as anti-ESG fund manager and Presidential candidate Vivek Ramaswamy created an anti-ESG proxy advisory firm[5] this year and it already has at least one major institutional investor client.[6]

   This is exactly how markets are supposed to work and it would be a catastrophic intrusion of the nanny state to interfere with a product that is purchased voluntarily by highly expert customers, just as they purchase many other independent research services to help them with investment decisions.

[4] https://www.proxyinsight.com/research/Proxy Insight PVA Research_151015023727.pdf
[5] https://strive.com/proxy-services/
[6] https://www.pionline.com/governance/pension-fund-nears-deal-anti-esg-firm-strive-proxy-voting-alternative

Further on the subject of proxy advisory firms: Up to 1986, there were no firms providing comprehensive proxy advisory services, just some specialty firms covering what today we would call social issues. In fact, ISS was not created to sell proxy advisory services. But when Bob Monks tried to sell the products we originally planned, no one wanted them. Instead, our prospective clients told us what they did want was independent advice on proxy proposals, which had suddenly become complex and controversial after decades of routine votes to re-elect the board and approve the audit firm.

That was the era of the hostile takeover, made possible by the invention of junk bonds that could finance even the largest acquisitions. And so, it was the era of abuse of investors by both raiders (as we called them in those days) and entrenched management (as we still call them). It was also the era of the rise of the institutional investor, pension funds and mutual funds, for example. And so, two powerful forces collided. For the first time there were widespread attacks on shareholder value and for the first time there were shareholders big enough to act, smart enough to know when it was necessary, and, as fiduciaries, obligated to do so when it was in the best interests of the beneficial holders.

There were some scandals, particularly the "Avon letter" matter, when the Department of Labor stepped in because CEOs were directing their pension funds to vote in favor of poison pills (rather, against shareholder proposals challenging poison pills), not because they were in the interests of the employee pension plan participants for whom the CEOs were acting as fiduciaries, but because they were in the interests of the CEOs themselves. This is the opposite of fiduciary obligation, and that is what the "Avon letter," dated February 23, 1988, addressed. Key points on ESG:

5. **There are no documented cases of ESG-based institutional investor decisions for any reason other than financial returns. But there are many documented cases of institutional investor decisions that favor corporate insiders due to commercial conflicts of interest with portfolio companies.** Big corporations, especially fossil fuel companies, have spent massive amounts of money to fight the E in ESG, with a lot of claims that ESG in general and E in particular leads to investment decisions, including proxy votes, that are not based exclusively on financial returns. And yet, in the many comments filed with the SEC and Labor Department, these commentors have been unable to come up with a single example of a buy-sell-hold or voting decision that is not based, to use the language of ERISA, on "the exclusive benefit" – meaning financial benefit – of the ultimate customer, whether a pension plan participant or mutual fund investor.

   There are many documented cases of decisions by fund managers that are contrary to the interests of beneficial holders. But these are not made for political or "woke" reasons; they are made for business reasons. As Vanguard founder John Bogle wrote many times over many years and as has been documented by studies going back to the 1980s, fund managers will vote proxies on, for example, CEO pay, contrary to the interests of

beneficial holders if the portfolio company is a current or potential client of the firm.[7] In one widely reported case, Deutsche Bank switched its vote on a business combination after a side payment from Hewlett Packard, resulting in an enforcement action by the SEC and the promulgation of the rules now requiring that votes be disclosed.[8]

6. **The Executive Branch and Independent Commissions at the federal level and state authorities for state and local funds already have not just the authority but the obligation to identify and bring enforcement actions if any institutional investors make any decisions for other than strictly financial returns, again, "for the exclusive benefit" of the beneficial holders.** That applies to all decisions relating to share ownership including buy-sell-hold, voting, or exercise of other share ownership rights including submitting shareholder proposals, nominating board members, and participating in shareholder litigation. As the "Avon letter" and Deutsche Bank examples cited above show, the government can and does enforce the obligation to act as fiduciaries. There is no evidence that further authority is required, though a reminder, with particular attention to the commercial conflicts issue, may be worth considering.

7. **There is no evidence that ESG-based investment decisions are based on non-financial criteria. On the contrary, ESG is a reflection of the inadequacy of traditional indicators in assessing investment risk and return.** It is not investors, either individual or institutional, who are proposing the weakening of financial measures of performance. The Business Roundtable announced in 2019 that their member corporations had agreed to work for vague "stakeholder"-oriented goals instead of shareholder value.[9]

   We have even seen admissions from corporations themselves that they object to ESG because they are looking for subsidies, not market-based investments. For example, a comment letter filed with the Labor Department by a trade association, The Western Energy Alliance first claimed that they support ESG, which one might think would lead them to conclude that they should be able to attract ESG-oriented investors. On the contrary, though, they then went on to say that they understand what ESG means better than pension fund fiduciaries, among the most sophisticated financial professionals in the world and subject to the strictest standards of care and loyalty our legal system imposes. Again, they failed to come up with a single example of a "wrong" or "non-pecuniary" or "political" investment decision by a pension fiduciary. Here is their real issue: "We have observed how ESG advocacy has negatively affected the industry's access to capital over the last few years." What the industry is saying here is that they want pension funds to subsidize otherwise market-unworthy investments. If ERISA directed plan fiduciaries to act for the exclusive benefit of corporate insiders, that might be worth considering. But an institutional investor fund manager's duty is to

[7] See for example: "Uncovering Conflict of Interest, As You Sow (https://www.asyousow.org/reports/uncovering-conflict-of-interest), Comment of John C. Bogle on File No. S7-36-02 (https://www.sec.gov/rules/proposed/s73602/jcbogle1.htm)

[8] https://www.sec.gov/news/press/2003-100.htm

[9] I disagreed. https://corpgov.law.harvard.edu/2019/09/02/six-reasons-we-dont-trust-the-new-stakeholder-promise-from-the-business-roundtable/

protect beneficial owners, and that is the opposite of what the Western Energy Alliance and the other critics of ESG are asking for.

In conclusion:

- Shareholder proposals are a very modest way to raise concerns at low cost to investors and to companies. They are submitted to a small fraction of companies but play an essential role in signaling concerns. If they are limited, the only options for shareholders will be far more disruptive and expensive.

- Proxy advisor services are not mandatory and are purchased by sophisticated financial experts. There are no barriers to entry as shown by the new "anti-woke" proxy advisory service, they are not unduly influential (as shown by the votes contrary to proxy advisor recommendations), and they are already adequately regulated.

- ESG indicators are a supplement to traditional financial disclosures, the ones that have repeatedly proven inadequate. Again, no one has to use them and they are purely market-driven. The only participants in these issues who have been driven by non-financial indicators are major corporations (the Business Roundtable's "stakeholder" pledge) and institutional investors (voting proxies to benefit portfolio companies who are clients instead of beneficial holders).

I am happy to provide additional information or answer any questions. And the attached appendices have further information about ESG and the deceptive dark money disinformation behind the opposition.

APPENDIX 1

Originally published by the NYU Law School Program of Compliance & Enforcement October 13, 2021

COMPLIANCE & ENFORCEMENT

Three Myths About ESG

by Nell Minow

ESG has passed the tipping point. For investors, ESG, which stands for Environmental, Social, and Governance factors, has gone from a nice-to-have to a have-to-have. ESG is the fastest growing area of investment, with every major financial institution and every significant institutional investor having one or more ESG options. U.S. ESG index funds reached over $250 billion in 2020. More significantly, ESG factors are permeating every aspect of even the most traditional investment vehicles. A 2020 survey of 809 institutional asset owners, investment consultants and financial advisers found that 75 percent of them use ESG factors in their investment strategies, up from 70 percent in 2019. Nearly 13 percent of respondents were pension plan sponsors. Corporate executives and board members are scrambling to catch up.

There are two major factors behind the new centrality of ESG. First, there is growing recognition that current financial reporting according to Generally Accepted Accounting Principles (GAAP) is not adequate. The upheavals of the dot-com bubble, the Enron-era accounting scandals, the 2008 financial meltdown, and the failed public offering of WeWork serve as reminders that there is a reason that accounting principles are called "generally accepted" and not "certifiably accurate." GAAP is fairly good at reporting the value of hard assets and computing present value of future income. It is less reliable in evaluating the worth of today's key assets like intellectual property and not of much use in informing investors about the asset almost all companies claim is their most valuable: their employees. GAAP is structured to externalize costs off the books as

much as possible, driving corporate strategy in that direction. ESG is about the information GAAP leaves out or underweights.

The second major factor is market-driven, based on demographics. Millennials and Generation Z are vastly more concerned with ESG issues like climate and social justice than their parents, harking back more to the boomer generation activism that led to the creation of the Environmental Protection Agency and other regulatory agencies devoted to health and safety concerns. As employees, consumers, and investors, they are insisting on better information and more explicit strategy relating to ESG.

The problem is that the market for ESG is far ahead of the ability to supply it. We are better at understanding the importance of ESG than we are at computing and understanding the data. There is no consensus and a lot of inconsistency in defining what ESG is. That has led to a lot of opportunistic grabs for fees and market share for services and products that are based on what can be counted, not on what counts. It has led to a lot of push-back from corporations and their service providers, as we see in the comments filed with the SEC in response to the Commission's request for feedback on climate change and ESG disclosures. And that includes messaging in support of myths designed to undermine legitimate efforts on ESG. Here are three of the most widely disseminated.

1. **ESG is new**. In the collection of The British Museum is a blue glass jar dating back to the early 19th century. The label identifies the company and the product: East India sugar. And then, in bigger letters, it has an ESG disclosure: "not made by SLAVES." The East India Company distinguished itself from its competition in the West Indies in response to the world's first grass-roots political movement and consumer boycott. This led to the abolition of slavery in the United Kingdom more than 30 years before it took a war to stop it in the United States. ESG is sometimes similarly dismissed as a fad. While fads are very popular in finance and investing, ESG is unlikely to disappear. It will continue to be refined, but it will not disappear. For example, the largest institutional investor in the U.S. is BlackRock, which has announced that 100 percent of its approximately 5,600 active and advisory BlackRock strategies are ESG integrated—covering U.S. $2.7 trillion in assets. Reflecting the demand, BlackRock introduced 93 new sustainable solutions in 2020, helping clients allocate U.S. $39 billion to sustainable investment strategies, which helped increase sustainable assets by 41 percent from December 31, 2019.
2. **ESG is monolithic.** It is critical to remember that ESG encompasses three enormous categories: environment, governance, and a catch-all category referred to as "social." Each is a moving target with constantly evolving ideas about what information is relevant and reliable and each has to be evaluated

separately. "Social" is the wild card in the group. Rising on the list in recent years are #MeToo and #BlackLivesMatter concerns. I predict that there will be increasing attention on political contributions and lobbying expenditures. This scrutiny has been catalyzed by reports from Judd Legum and others about contributions companies have made contrary to their public commitments not to donate to elected officials who supported the January 6 insurrection or who get poor ratings from women's and racial equity groups.

3. **ESG is "non-pecuniary"—adjacent to or conflicting with financial goals.** This was the explicit underlying assumption in the now-suspended ESG rule pushed through the Department of Labor in the last weeks of the Trump administration, directed at pension fiduciaries. The suspension of the rule as the Biden administration examines the issues is based on two key facts. First, the Department already has not just the enforcement authority but the obligation to use it if a pension fiduciary makes an investment decision for any reason other than "the exclusive benefit of plan participants." Second, the proponents of the anti-ESG rule failed to come up with a single example of any investment made by any fiduciary for other than purely financial reasons. There is a lot still to be determined about ESG and some arguments to be had over long-and short-term calculations, but it is always financial.

ESG is like the use of the term "organic." Consumer demand has led to unsupported claims, and it is time for the government to establish clear, consistent, and credible guidelines. In the meantime, companies should increase their disclosures about the procedures they have established for self-evaluation on ESG and what their priorities and goals are, putting some reality into a term with too many myths.

Nell Minow is Vice Chair of ValueEdge Advisors, a corporate governance consulting firm. She was previously General Counsel and President of Institutional Shareholder Services, a principal of the activist LENS Fund, and a partner in GMI Ratings. She writes frequently about corporate governance issues.

APPENDIX 2

We recognize that ESG is still an evolving discipline. But it is not a fad. ESG has passed the tipping point. For investors, it has gone from a nice-to-have to a have-to-have. ESG is the fastest growing area of investment, with every major financial institution and every significant institutional investor having one or more ESG options. US ESG index funds reached over $250 billion in 2020. More significantly, ESG factors are permeating every aspect of even the most traditional investment vehicles. A 2020 survey of 809 institutional asset owners, investment consultants and financial advisers[10] found that 75 percent of them use ESG factors in their investment strategies, up from 70 percent in 2019. Nearly 13 percent of respondents were pension plan sponsors. Corporate executives and board members are scrambling to catch up.

There are two major factors behind the new centrality of ESG. The first is the growing recognition that current financial reporting according to GAAP is not adequate. The upheavals of the dot.com bubble, the Enron-era accounting scandals, the financial meltdown, the failed public offering of WeWork and so much more remind us that there is a reason that accounting principles are called "generally accepted" and not "certifiably accurate." GAAP is fairly good at reporting the value of hard assets and computing present value of future income. It is less reliable in evaluating the worth of today's key assets like intellectual property and not of much use in informing investors about the asset almost all companies claim is their most valuable: their employees. GAAP is structured to externalize costs off the books as much as possible, driving corporate strategy in that direction. ESG is about the information GAAP leaves out or underweights.

The second major factor is market-driven, based on demographics. Millennials and the generation that follows them are vastly more concerned with ESG issues like climate and social justice than their parents, harking back more to the boomer generation activism that led to the creation of the Environmental Protection Agency, OSHA, and other regulatory agencies devoted to health and safety concerns. As employees, consumers, and investors, they are insisting on better information and more explicit strategy relating to ESG.

The problem is that the market for ESG is far ahead of the ability to supply it. We are better at understanding the importance of ESG than we are at computing and understanding the data. There is no consensus and a lot of inconsistency in defining what ESG is. That has led to a lot of opportunistic grabs for fees and market share for services and products that are based on what can be counted, not on what counts. It has led to a lot of push-back from corporations and their service providers, including efforts to distort the market by promoting restrictions on ESG-based assessments. Th answer is not to try to ignore the growing understanding of ESG factors, just to be clear that pension fiduciaries have to evaluate them with the same due diligence they bring to other data about investment risk and return.

ESG is nothing new. In the collection of The British Museum is a blue glass jar dating back to the early 19th century. The label identifies the company and the product: East India sugar. And then, in bigger letters, it has an ESG disclosure: "not made by SLAVES." The East India Company distinguished itself from its competition in the West Indies in response to the world's first grass-roots political movement and consumer boycott. This led to the abolition of slavery in the United

[10] https://www.pionline.com/esg/esg-integration-grows-globally-does-gap-between-us-and-others-survey

Kingdom more than 30 years before it took a war to stop it in the United States. ESG is sometimes similarly dismissed as a fad. While fads are very popular in finance and investing, ESG is unlikely to disappear. It will continue to be refined, and its influence will increase. For example, the largest institutional investor in the US is Black Rock, which has announced that 100 percent of its approximately 5,600 active and advisory BlackRock strategies are ESG integrated – covering U.S. $2.7 trillion in assets. Reflecting the demand, BlackRock introduced 93 new sustainable solutions in 2020, helping clients allocate U.S. $39 billion to sustainable investment strategies, which helped increase sustainable assets by 41 percent from December 31, 2019. As it consistently has throughout its history, EBSA's assessment of pension fiduciaries making ESG investments should be based on process and due diligence rather than results.

ESG is not monolithic. It is critical to remember that ESG encompasses three enormous categories: environment, governance, and a catch-all category we call social. Each is a moving target with constantly evolving ideas about what information is relevant and reliable and each has to be evaluated separately. "Social" is the wild card in the group. Rising on the list in recent years are #metoo and #blacklivesmatter concerns, plus increasing attention on political contributions and lobbying expenditures following news stories from Judd Legum[11] and others about contributions contrary to public statements about ending funding for elected officials who supported the January 6 insurrection or to those who get poor ratings from women's groups and racial equity groups. EBSA should be careful to make sure that its rules promote rather than restrict the development of ESG metrics.[12]

ESG is never "non-pecuniary" – adjacent to or conflicting with financial goals. None of the corporate executive and trade associations have documented a single example of a pension fiduciary making any financial trade-off in ESG-qualified investments. Quite the contrary. It is a reflection of the increasing recognition, following the dot.com collapse, the Enron era accounting failures, the security analyst corruption scandal, the financial meltdown, and many other examples, showing the inadequacy of GAAP in estimating investment risks and returns. GAAP is still based in 19th century notions and is better at estimating the value of property, equipment, and other hard assets than it is at valuing what most corporations claim is their most important asset, human capital. ESG can provide significant data about employee turnover, the resources devoted to employee development and education as well as information about compliance with regulatory risk relating to climate change and other E, S, and G issues.

To provide some context for these concerns, here are just a few of the extensive and compelling developments and evidence on ESG as a meaningful risk factor, many from the Trump administration, that not only can but must be a part of any fiduciary's responsibility to evaluate and act on:

1. The Environmental Protection Agency[13] published a 150-page document about coping with the debris from natural disasters across the country, which said, "Start planning for the fact that climate change is going to make these catastrophes worse. This is an essential issue for every element of

[11] https://popular.info

[12] https://www.responsible-investor.com/articles/i-want-to-make-an-official-request-of-regulators-and-the-esg-community-stop-it

[13] https://www.epa.gov/homeland-security-waste/guidance-about-planning-natural-disaster-debris

corporate strategy, from supply chain issues to core operations and risk management." EPA also has a sustainability initiative[14] on better disclosure of investment risk.

2. A study published in *Sustainability Accounting, Management and Policy Journal* by Michael Magnan and Hani Tadros[15] found that better disclosure of environmental performance correlated with better performance at the 78 companies in environmentally sensitive industries that they examined.

> In this paper, we aim to bridge the gap in the literature about the association between environmental disclosure and environmental performance by analyzing the motivation of firms with high or low environmental performance to disclose proprietary environmental information that could compromise the firm's competitive position or have direct impact on its cash flow. Consistent with some prior research, we argue that economic- and legitimacy-based incentives both drive a firm's environmental disclosure. However, revisiting prior research, we put forward the view that a firm's environmental performance (either high or low) moderates the effects of these incentives on environmental disclosure in a differential fashion.

Of course, you do not have to be an economist to conclude that companies will be more transparent when there is good news to report. What matters here is what investors can conclude from the level of transparency in these disclosures, and what it means about the potential – or necessity – for engagement. We point the Committee to the work of Tensie Whelan of NYU Stern Center for Sustainable Business on ESG data as a key indicator of supply chain risk, relating to the State Department release cited below.

3. The Bank of England takes note of climate-related investment risk:

> [A] speech by Sarah Breeden,[16] head of international banks supervision, suggests...that time is running out to prevent catastrophic climate change and previous efforts to combat the problem have been nowhere near vigorous enough.
>
> Breeden's message to the financial sector was that they need to incorporate climate change into their corporate governance, their risk management analysis, their forward planning and their disclosure policies or face the prospect of losing a heck of a lot of money.
>
> The financial markets have a term for a sudden drop in assets prices known as a Minsky moment (after the economist Hyman Minsky). Breeden said a climate Minsky moment was possible, in which losses could be as high as $20tn (£15.3tn).

If the Bank of England is calling on companies to address the risks of climate change, then the Department of Labor should recognize that pension fund managers' similar assessment of risk is consistent with their obligation as fiduciaries.

---

[14] https://www.epa.gov/sites/default/files/2019-12/documents/esgmetricsreportingtemplate_pam_lacey.pdf
[15] https://www.emerald.com/insight/content/doi/10.1108/SAMPJ-05-2018-0125/full/html
[16] https://www.bankofengland.co.uk/-/media/boe/files/speech/2019/avoiding-the-storm-climate-change-and-the-financial-system-speech-by-sarah-breeden.pdf

4. A July 2020 report from GAO[17] documents the financial/"pecuniary" priority of institutional investors use of ESG factors in calculating investment risk. We incorporate that entire report by reference in this document. An excerpt:

> Institutional investors with whom we spoke generally agreed that *ESG issues can have a substantial effect on a company's long-term financial performance*. All seven private asset managers and representatives at five of seven public pension funds said they seek ESG information *to enhance their understanding of risks* that could affect companies' value over time. Representatives at the other two pension funds said that they generally do not consider ESG information relevant to assessing companies' financial performance. While investors with whom we spoke primarily used ESG information to assess companies' long-term value, other investors also use ESG information to promote social goals. A 2018 US SIF survey found that private asset managers and other investors, representing over $3.1 trillion (of the $46.6 trillion in total U.S. assets under professional management), said they consider ESG issues as part of their mission or in order to produce benefits for society....
>
> These investors added that they use ESG disclosures to monitor companies' management of ESG risks, inform their vote at shareholder meetings, or make stock purchasing decisions. Most of these institutional investors noted that they seek additional ESG disclosures to address gaps and inconsistencies in companies' disclosures that limit their usefulness. [emphasis added, footnotes omitted]

Not one of the investors surveyed made any "pecuniary" trade-offs and the overwhelming majority look at ESG exclusively in financial terms.

5. Pensions and Investments[18] reported on an ISS study:

A link exists between a company's ESG performance and its financial performance, according to a study published from ISS ESG, the responsible investment arm of Institutional Shareholder Services.

Firms with high or favorable ISS ESG corporate ratings tend to be more profitable through an economic value-added lens, the study found.

> While one can argue that the relationship between ESG and financial performance is perhaps due to the fact that more profitable firms have the resources to invest in areas that positively influence ESG, it could also be that profitability rises as a result of a company better managing its material ESG risks, or it could be a little bit of both," the study said. "If it is a little bit of both, then this means that good-ESG initiatives drive up financial performance, which then provides the monetary resources to invest to be an even better ESG firm, which then drives up performance again, and so on.

[17] https://www.gao.gov/assets/710/707949.pdf
[18] https://www.pionline.com/esg/iss-study-links-esg-performance-profitability

Moreover, companies with better ESG ratings are also less volatile, noted Anthony Campagna, global head of fundamental research at ISS EVA.

6. Corporations are increasingly providing ESG disclosures[19] to respond to investor demand and to assist in their own strategic planning, and those that do tend to outperform. Whether that is cause or effect is not clear, but for investment risk assessment purposes, that makes little difference.

Since July 2017, following the release of the Task Force on Climate Related Disclosure (TCFD) guidelines, more than 500 large businesses, investors and industry groups have signed on to provide this type of forward-looking financial disclosure. Companies in the financial services industry are leading the way in their support of the TCFD recommendations, including BlackRock, State Street and S&P Global, along with the Association of Chartered Certified Accountants.

It is not limited to the financial services industry. Other sectors are signing on, including Statoil and Shell in the energy sector, consumer product companies such as H&M and Nestlé, materials companies such as BASF and DowDuPont, as well as industrial companies such as Saint-Gobain and Ingersoll Rand.

7. On July 1, 2020 the U.S. Department of State, along with the U.S. Department of the Treasury, the U.S. Department of Commerce, and the U.S. Department of Homeland Security issued a business advisory to caution businesses about the risks of supply chain links to entities that engage in human rights abuses, including forced labor, in the Xinjiang Uyghur Autonomous Region (Xinjiang) and elsewhere in China. DOI/EBSA should not issue a rule that fundamentally undermines this critical policy advisory from four other Departments. EBSA should coordinate with the other federal agencies to ensure that pension fiduciaries are not discouraged from making the appropriate calculations about supply chain risk.

8. A new global alliance of financial institutions, investors and businesses,[20] is launching a new central source for accessible, digital, corporate sustainability information in support of the 10 principles of the UN's Global Compact.[21]

9. President Biden's wide-ranging initiatives on ESG issues include an Executive Order on Climate-Related Financial Risk.[22] As the Department is aware, it will impose new obligations and create new opportunities for assessing investment risk based on climate and other ESG factors.

> It is therefore the policy of my Administration to advance consistent, clear, intelligible, comparable, and accurate disclosure of climate-related financial risk (consistent with Executive Order 13707 of September 15, 2015 (Using Behavioral Science Insights to Better Serve the American People)), including both physical and transition risks; act to mitigate that risk and its drivers, while accounting for and addressing disparate impacts on

[19] https://www.greenbiz.com/report/2019-state-green-business-report
[20] https://www.ft.com/content/304f9a1f-cb31-4c83-81bd-d814aa211c26
[21] https://www.unglobalcompact.org
[22] https://www.whitehouse.gov/briefing-room/presidential-actions/2021/05/20/executive-order-on-climate-related-financial-risk/

> disadvantaged communities and communities of color (consistent with Executive Order 13985 of January 20, 2021 (Advancing Racial Equity and Support for Underserved Communities Through the Federal Government)) and spurring the creation of well-paying jobs; and achieve our target of a net-zero emissions economy by no later than 2050. This policy will marshal the creativity, courage, and capital of the United States necessary to bolster the resilience of our rural and urban communities, States, Tribes, territories, and financial institutions in the face of the climate crisis, rather than exacerbate its causes, and position the United States to lead the global economy to a more prosperous and sustainable future.

Another Executive Order focuses on creating opportunities for clean energy[23] that will affect the investment risk assessment in many sectors.

10. "ESG: Shareholder Engagement and Downside Risk"[24] finds that "successful engagement [on ESG factors] reduces the firm's exposure to a downside-risk factor."

11. In the Harvard Business Review article, An ESG Reckoning is Coming[25], Michael O'Leary and Warren Valdmanis write that companies have been better at promising to meet ESG goals than delivering on them, which underscores the vital importance of shareholder oversight to protect loss of shareholder value.

12. The SEC's Asset Management Advisory Committee recommended meaningful, consistent, and comparable disclosure of material environmental, social, and governance ESG disclosures earlier this year.[26] Increasing adoption of TCFD[27] and SASB[28] disclosure standards will provide critical information for all investors, including pension fiduciaries, to factor into their assessments of investment risk.

13. In Fortune Magazine, Professor Jeffrey Sonnenfeld and Steven Tian extensively document the superior performance of ESG-enhanced funds over the anti-ESG funds.[29]

14. If you shorted the companies led by the top ten most over-paid CEOs, you would outperform the market.[30] That's one of the most important elements in the G of ESG.

---

[23] https://www.whitehouse.gov/briefing-room/presidential-actions/2021/12/08/executive-order-on-catalyzing-clean-energy-industries-and-jobs-through-federal-sustainability/

[24] https://www.researchgate.net/profile/Xiaoyan-Zhou-7/publication/318002428_ESG_Shareholder_Engagement_and_Downside_Risk/links/5e6769ce299bf1744f6f12f6/ESG-Shareholder-Engagement-and-Downside-Risk.pdf

[25] https://hbp.az1.qualtrics.com/CP/File.php?F=F_e4XeHWSIIMVXsRo

[26] https://www.sec.gov/files/amac-recommendations-esg-subcommittee-070721.pdf

[27] https://www.fsb-tcfd.org

[28] https://www.sasb.org

[29] https://fortune.com/2023/06/05/alt-right-economy-is-failing-real-performance-of-anti-woke-entrepreneurs-business-politics-sonnenfeld/

[30] https://www.asyousow.org/reports/the-100-most-overpaid-ceos-2023

15. Even Vivek Ramaswamy, the Presidential candidate who has devoted his entire career to opposing "woke" investments and ESG puts his own money into ESG-friendly companies.[31] The founder of the anti-ESG Strive fund does not puts his own money where his mouth is.

[31] https://www.nytimes.com/2023/07/07/us/politics/vivek-ramaswamy-wealth-plane.html

APPENDIX 3

May 17, 2023

Hon. Richard Revesz
Administrator
Office of Information and Regulatory Affairs
U.S. Office of Management and Budget
725 17th St NW
Washington, D.C. 20053

Re: OMB–2022–0014

Dear Administrator Revesz:

I am an OIRA alum. I was there almost from the beginning, arriving in 1981, when Jim Miller was heading the office. I had come from EPA, where I learned a lot about notice-and-comment regulation, including the conflicts that arose from failure to coordinate between agencies. I recall there was one toxic substance that was regulated separately and often inconsistently depending on whether it was being transported on the highways, transported by trains, exposed to people in the workplace, exposed to people at home through consumer products, or being left in garbage dumps. I also saw the wide disparity in application of cost-benefit analysis and access to the best examples in categories like performance standards vs. design standards, failure to comply with the Paperwork Reduction Act, and lack of consistency in trying to find a balance between clarity and flexibility.

Working at a regulatory agency and then at OIRA gave me both a trees and forest look at domestic rulemaking and notice and comment proceedings. OIRA was one of the greatest experiences of my professional life, helping to make essential, life-improving regulations work better – and get rid of ones that were outdated. I have the greatest respect for the diligence, expertise, and integrity of the agency employees who develop regulations, but the role OIRA plays as clearinghouse and providing coordination and oversight is essential.

When I arrived at OIRA, desk officers did not even have desktop computers; we worked on electric typewriters. It has come a long way. It has been a deep source of satisfaction to see the office play a vital and broadly welcomed role in the regulatory process, through many different administrations.

I was very glad to see these proposed guidelines, which are very much in line with what I know of OIRA's perspective and function. I would like to raise an additional question, based on my experience since I left OIRA in participating in about a dozen rulemakings at different agencies through comments and testimony, always sharing my own views, as I do in this letter, with my employer only as identification, never on behalf of a client.

In recent years, I have increasingly been struck by the problem of dark money-funded "astroturf" (fake grassroots), fake "public policy" thinktanks[33], fishy" comments[34], sock puppets,[35] and advocacy masquerading as scholarship that are seriously undermining the integrity of the notice and comment system.

Until a few years ago, I believed that the notice and comment process worked remarkably well, giving government agencies and independent commissions a chance to be guided by the experts who must comply with regulations and minimizing the problem of unintended consequences. It has been less effective in preventing regulatory capture, but overall it has struck a good balance by making the interactions between the regulators and the regulated transparent.

That is no longer true. Corporations and billionaires have set up dozens, maybe hundreds of fake groups with generic names that file comments without disclosing their sources of funding. They cite each other without disclosing their connections, not just their funders but often their executives as well. They have even gone so far as to submit comments with forged signatures, purportedly from individuals but in reality drafted by K Street "communications" firms. These firms have created fake "news" websites and fake social media profiles. For one of the rulemakings I commented on, at the SEC, they even posted a YouTube video,[35] again not disclosing that it was paid advocacy, warning viewers (falsely) that if a proposed SEC regulation on proxy advisory firms did not go final it would usher in open borders, gun control, and abortion. There are many, many more examples, and I would be happy to meet with staff (and have that meeting added to the record of this rulemaking) if it would be useful.

Without disclosure about the sources of the comments, the entire system is distorted. The clients and funders are essential for assessing the credibility of the comment. They know that, and that is why these dark money-funded fake front groups are created specifically to hide the money behind them. If a "study" is done by the industry or by an advocacy group, it should be viewed differently than if it is done by a non-partisan independent organization or an academic who does not receive funding from an affected party. They know it matters; that is why they hide it. You do not have to be an economist to understand that incentives make a difference. A comment from a group that tries to hide its funders should be viewed with skepticism.

The rules that apply in so many other areas of communication to prevent misleading and outright fraudulent information are not in force here. The generically-named Texas Public Policy Foundation, which cherry-picks data to pretend climate change is not a problem, does not mention that its funders include energy companies Chevron, ExxonMobil, and other fossil fuel interests.[36]

---

[33] https://www.nytimes.com/2020/11/11/climate/fti-consulting.html

[34] https://www.bloomberg.com/news/articles/2019-11-19/sec-chairman-cites-fishy-letters-in-support-of-policy-change

[35] https://valueedgeadvisors.com/2018/11/06/more-useless-sock-puppet-bluster-from-fake-front-group-main-street-investor-coalition/ and note the overlap in the comments between groups with the same members/funders like the Business Roundtable and the World Business Council.

[35] https://valueedgeadvisors.com/2020/01/10/republican-operative-holly-turner-posts-appallingly-deceptive-video-in-support-of-anti-shareholder-proposal-from-the-sec/

[36] Their use of the inaccurate and inapposite term "cartel" to describe the proxy contest at ExxonMobil is a hint of their lack of credibility as well. One would think that they might conclude the successful election of three dissident

The FreedomWorks comment is especially misleading because it is "signed" by a long list of anonymous individuals (last names omitted), but fails to disclose that the group is funded by major corporations and groups related to the ultra-wealthy, anti-regulation Scaife and Koch families. These are material omissions because basic law and economics make clear that knowing who is paying for a source is necessary to evaluate its purpose and objectivity.

The fix is easy, and the cost is negligible. All it would take is the addition of language like this in any notice of proposed rulemaking:

> We encourage commenters to state clearly whether they are receiving payment or subsidies, directly or indirectly, for submission of the comment and any financial ties they have to those who are likely to be affected by the rule. These disclosures are not required but failure to include them will be a factor in determining the credibility of the comments.

I also ask that before agreeing to any meeting OIRA staff or political appointees have with outside groups to discuss pending regulatory proposals, the group or representative be asked to state for the record their funders or clients. As you know, groups like Donors Trust (that calls itself "the community foundation for liberty" but is called by critics the Koch-funded "ATM for the far right") hide behind names that are intentionally vague, blandly institutional, and faintly patriotic. They often represent the opposite of what their names suggest. For example: Judicial Education Project, The Fairness Center, Americans for Prosperity Foundation, Committee for a Constructive Tomorrow, Commonwealth Foundation for Public Policy Alternatives, Franklin Center for Government and Public Integrity, Independent Women's Forum, Heartland Institute, National Center for Public Policy Research, Consumers' Research, Institute for Humane Studies, etc. etc. I am not aware of any similarly obfuscatory efforts from progressive/liberal sources, but should there be, of course my concerns apply equally to them as well or any group that fails to disclose their direct and indirect sources of funding.

I met with just one such group when I was an OIRA desk officer, represented by a man who insisted that he was just working on his own for his love of animals. He was so specific about the LD50 tests that I questioned him further. He turned out to be funded by pharma companies trying to reduce animal testing requirements. Since then, efforts like these have grown to overtake Executive Branch and independent agency rulemaking. They have permeated and undermined the notice and comment process and the federal and state level. I urge OIRA, as the quality control on the conveyer belt of federal regulation, to address this issue to minimize the damage these fake front groups are causing.

I note that at this writing, the REIN legislation is included in the debt ceiling bill passed by the House. I do not think it will pass the Senate. But it is still worthwhile to express my concern that if it ever did become law, it would create chaos for the administrative and independent agencies. I trust that the White House legislative affairs office is raising these concerns.

My thanks to you and the staff for an excellent proposal, reflecting OIRA's outstanding professionalism. If I can be of any assistance, please do not hesitate to call on me.

---

directors was an indicator of investor frustration at the inadequacy of the company's communications about climate change (as well as its $22 billion loss last year).

NATIONAL ASSOCIATION OF Manufacturers

Testimony of

Chris Netram
Managing Vice President, Policy
National Association of Manufacturers

Before the

U.S. House of Representatives
Committee on Financial Services
Subcommittee on Capital Markets

Hearing on

"Reforming the Proxy Process to Safeguard Investor Interests"

July 13, 2023

Good morning Chairwoman Wagner, Ranking Member Sherman and members of the Subcommittee on Capital Markets. My name is Chris Netram, and I am the Managing Vice President of Policy at the National Association of Manufacturers. On behalf of the NAM and the millions of people who make things in America, I appreciate the opportunity to testify before today's Subcommittee hearing on *Reforming the Proxy Process to Safeguard Investor Interests*.

The NAM is the largest manufacturing association in the United States, representing nearly 14,000 manufacturers of all sizes and in every industrial sector. Manufacturers are dedicated to creating products and processes to improve the quality of life for all Americans; every day, innovators throughout our industry pioneer groundbreaking new technologies and celebrate America's entrepreneurial spirit.

When the manufacturing industry succeeds, America succeeds. Manufacturers employ nearly 13 million Americans from all walks of life, paying $95,990 on average in wages and benefits. Manufacturing's annualized contribution to the U.S. economy was $2.9 trillion as of the first quarter of 2023; by itself, manufacturing in the U.S. would be the eighth-largest economy in the world. And manufacturers are continuing to invest in growth—monthly construction spending in the industry rose to a record $193.88 billion in May of this year—while performing more than 55% of all private-sector research and development. This growth bolsters U.S. competitiveness on the world stage, especially as China continues to work toward its ambition of becoming the world leader in advanced manufacturing.

Manufacturing is a capital-intensive industry. As such, the industry's strength depends in large part on companies' ability to raise the funds necessary for critical investments in equipment, machinery, facilities and R&D. Many manufacturers turn to the public market to access this capital, which supports job-creating projects and robust partnerships with businesses of all sizes, including small and medium-sized businesses, throughout the manufacturing supply chain.

When manufacturers offer their shares to the public, it allows everyday Americans to participate in the industry's success, largely through passive investments like mutual funds, pension plans and 401(k) accounts. The fiduciary relationship between publicly traded companies and their

shareholders lies at the bedrock of America's world-leading capital markets. Manufacturers' management teams and boards of directors must act in Main Street investors' long-term financial best interests, and those investors have the right to hold company leaders accountable via the proxy ballot.

The proxy process historically has been governed by state law, with required proxy votes generally limited to significant items like the election of the board of directors or referenda on the sale of substantially all of a corporation's assets. These votes allow a shareholder to exercise appropriate oversight of a company while also ensuring that its board and management can act, consistent with their fiduciary duty, in the financial best interests of the entire shareholder base.

Unfortunately, in recent years manufacturers have experienced an influx of third parties seeking to divert the proxy ballot from long-term value creation for shareholders and toward a political and social agenda with little if any nexus to a company's business. This parade of activist groups and proxy advisory firms are enabled by a lack of appropriate regulatory oversight from the Securities and Exchange Commission. In fact, the SEC over the past two years has taken proactive steps to support and empower these third-party actors—rescinding much-needed guardrails, limiting companies' ability to exclude activist proposals from the proxy ballot and encouraging environmental, social and governance agendas unrelated to long-term business growth and shareholder returns. These changes are emblematic of the regulatory onslaught that manufacturers are currently experiencing from all corners of the federal government.

The increasing politicization of the proxy ballot has a significant impact on manufacturing. For businesses, each shareholder proposal imposes direct costs in excess of $150,000,[1] to say nothing of the public relations risks associated with being pressured to opine on controversial topics over which they have little control. Those funds would be more efficiently utilized investing in job-creating projects and groundbreaking R&D, especially as companies receive more and more proposals each year, driving up the aggregate cost. Every dollar spent on manufacturing investment has a total impact of $2.60 on the U.S. economy, and every job created in manufacturing leads to 4.4 jobs elsewhere—so the resource diversion associated with publishing and responding to activist proposals can be particularly damaging in our industry. These impacts are particularly acute for smaller businesses, both those directly impacted by ESG activists and those operating within public companies' supply chains.

In addition to these risks to manufacturing growth and job creation, manufacturing workers also are impacted because many have a stake in the industry via employer-sponsored retirement plans or other investment accounts. More than 70% of manufacturing employees participate in a workplace retirement plan,[2] and the ability of a single-issue activist with *de minimis* holdings in a business to dictate the content of its proxy ballot and exercise outsized influence on its corporate decision-making can only threaten these employees' financial stability and retirement security—especially given that studies have shown that ESG proposals can detract from shareholder value.[3]

---

[1] House Report No. 115-904, to accompany H.R. 5756. House Committee on Financial Services, 115th Congress, 2nd Session (24 August 2018).

[2] *National Compensation Survey: Employee Benefits* (May 2022). Bureau of Labor Statistics. *Available at* https://www.bls.gov/ebs/publications/september-2022-landing-page-employee-benefits-in-the-united-states-march-2022.htm.

[3] Joseph P. Kalt, L. Adel Turki et al., *Political, Social, and Environmental Shareholder Resolutions: Do They Create or Destroy Shareholder Value?* (June 2018). *Available at* https://documents.nam.org/tax/nam_shareholder_resolutions_study.pdf.

To be clear, manufacturers believe strongly in the importance of combatting climate change, ensuring sustainable business operations and enhancing diversity, equity and inclusion in the workforce.

- For example, a recent survey of senior manufacturing executives conducted by the Manufacturing Leadership Council, the NAM's digital transformation division, found that 90% of respondents believed that manufacturing has a special responsibility to society to become more sustainable.[4] And companies are putting this belief into action—manufacturing in the U.S. is cleaner and more sustainable today than at any other time in history due to a revolution in how manufacturers produce, use and recycle energy. Thanks to these improvements, the U.S. reduced the six most common air quality pollutants by 78% between 1970 and 2020.[5] Looking forward, 90% of manufacturers are focused on improving energy efficiency and reducing energy use, 85% have a company-wide strategy to address sustainability or have embedded sustainability into their business practices and 57% either have or are developing a net zero greenhouse gas emissions-reduction goal.[6]

- Similarly, a recent report by the Manufacturing Institute, the NAM's workforce development and education affiliate, showed that a majority of manufacturing leaders believe that efforts to enhance diversity, equity and inclusion are critical to attracting, retaining and developing talent.[7] Manufacturing leaders have also found that DEI efforts can increase productivity, ensure balanced organizational management and increase their competitive advantage.[8] These efforts are critical at a time when there are 604,000 open jobs in manufacturing waiting to be filled.[9]

In short, manufacturers are already taking steps to address these important issues in a way that is appropriate for their businesses—not because it might result in a high ESG rating from an activist group, but because it is the right thing to do for their workers, their shareholders and the U.S. economy as a whole. ESG activists and their allies have no such duty to everyday American investors, and so are free to pursue social and political outcomes divorced from the best interests of a business and its shareholders. Recent actions from the SEC have only served to further empower these groups.

Today's Subcommittee hearing on the proxy process thus comes at a critical time. Congressional action is needed to counter the outsized influence that politically motivated third-parties have on the proxy process and to depoliticize the business decisions that impact the lives and life savings of millions of Americans. Addressing these important issues will drive job-creating investments throughout the manufacturing industry, support a robust manufacturing supply chain in local communities across the country and bolster American manufacturing competitiveness on the world stage.

---

[4] *Survey: Sustainability Momentum Surges Dramatically* (29 November 2022). Manufacturing Leadership Council. *Available at* https://www.manufacturingleadershipcouncil.com/survey-the-sustainability-shift-accelerates-31159/.

[5] *Our Nation's Air* (8 June 2020). Environmental Protection Agency. *Available at* https://gispub.epa.gov/air/trendsreport/2020/#home.

[6] MLC Sustainability Survey, *supra* note 4.

[7] *Beyond reskilling: Manufacturing's future depends on diversity, equity, and inclusion* (4 May 2021). Deloitte and the Manufacturing Institute. *Available at* https://www.themanufacturinginstitute.org/wp-content/uploads/2021/05/us-dei-beyond-reskilling.pdf.

[8] *Ibid.*

[9] *Job openings levels and rates by industry and region, seasonally adjusted* (6 July 2023). Bureau of Labor Statistics. *Available at* https://www.bls.gov/news.release/jolts.t01.htm.

To ensure that manufacturers can focus on creating value for shareholders and driving economic expansion in the United States, the NAM is calling on Congress to:

1. Prevent activists from hijacking the proxy ballot in pursuit of agendas unrelated to long-term business growth and shareholder value creation;
2. Rein in proxy advisory firms and limit their outsized influence on corporate governance;
3. Reinforce asset managers' fiduciary duty to Main Street investors and retirees; and
4. Address the onslaught of ESG disclosure mandates by requiring public companies to report only that information which is material to their shareholders.

The NAM appreciates that the Subcommittee is considering legislation today that would accomplish these critical goals. Manufacturers are dedicated to protecting the Americans who have entrusted them with their hard-earned savings and who depend on those investments for their retirement and quality of life. The NAM looks forward to working with the Subcommittee to advance the following bills to rein in the SEC's regulatory overreach, keep activists out of the boardroom and protect Americans' investments in manufacturing growth.

I. Depoliticizing Corporate Governance

Modern portfolio theory, which prioritizes diversification to protect against downside risk, means that most Main Street investors hold shares in dozens if not hundreds of companies—whether individually or through investing vehicles like mutual funds. It is simply not practical for shareholders to be involved in the day-to-day operations of each of these companies. Instead, investors depend on corporate leadership to act in their long-term financial best interests by increasing the value of the business and thus enabling everyday Americans to save for retirement, a new home or a child's education.

The proxy ballot protects shareholders by granting them oversight of the company leaders who are charged with safeguarding their investments. But activist groups have hijacked the ballot in pursuit of political agendas unrelated to long-term business growth and shareholder value creation.

The NAM has long supported reforms to Rule 14a-8—which dictates which shareholder proposals companies must include on their proxy ballot—in order to protect the integrity of the proxy process and limit activists' influence. In 2020, manufacturers supported[10] an SEC rule to increase the share ownership thresholds under Rule 14a-8 that enable activists to take *de minimis* positions in a company's stock for the sole purpose of forcing the entire shareholder base to consider a politically motivated proposal.[11] The 2020 rule also increased Rule 14a-8's resubmission thresholds, which allow activists to place a proposal on the proxy ballot year after year, even when it has been resoundingly rejected by the vast majority of shareholders.

Unfortunately, the SEC recently has taken steps to undermine these critical reforms and to empower activists at the expense of public companies and their long-term shareholders. In 2021, the SEC's Division of Corporation Finance issued Staff Legal Bulletin 14L, which effectively prohibits companies from excluding from the proxy ballot any shareholder proposal related to environmental and social topics of "broad societal impact."[12] The 2020 rule was designed to prioritize the needs of

[10] NAM Comments on Proposed Amendments to Rule 14a-8 (3 February 2020). *Available at* https://documents.nam.org/tax/namshareholderrulecomments.pdf.

[11] *Procedural Requirements and Resubmission Thresholds Under Exchange Act Rule 14a-8*, 85 Fed. Reg. 214 (4 November 2020). Release No. 34-89964; *available at* https://www.govinfo.gov/content/pkg/FR-2020-11-04/pdf/2020-21580.pdf.

[12] *Staff Legal Bulletin No. 14L* (3 November 2021). SEC Division of Corporation Finance. *Available at* https://www.sec.gov/corpfin/staff-legal-bulletin-14l-shareholder-proposals.

long-term shareholders over the agendas of activist investors—but SLB 14L effectively grants activists special access to the proxy ballot to pursue ESG causes of their choosing. The NAM has said that SLB 14L will "incentiviz[e] shareholder proposals wholly unrelated to long-term shareholder value creation" and transform the proxy process "into an avenue for activists to apply pressure to companies on the political issues of the day."[13]

Similarly, in 2022 the SEC proposed a rule that would significantly narrow several of the so-called "exclusion criteria" under Rule 14a-8.[14] These criteria allow companies to exclude from the proxy ballot proposals that would divert time and resources by forcing shareholders to consider irrelevant, inappropriate, moot, duplicative or unlawful proposals. But the SEC's proposed rule is designed to make it more difficult for companies to exclude proposals that have already been substantially implemented by the company, are duplicative of other proposals on a given year's proxy ballot or have been rejected by a large percentage of the shareholder base in previous years—making it easier for activists to flood the proxy ballot with these substantially implemented, duplicative and resubmitted proposals.

Activists have received the SEC's message loud and clear. During the 2022 proxy season, shareholder proponents once again submitted a record-breaking number of proposals, continuing a persistent trend from the last several years.[15] Fully 60% of the proposals ultimately included on companies' proxy ballots involved environmental or social issues, an all-time high.[16] Environmental proposals were up 51% as compared to 2021, while lobbying and political spending proposals increased 36% and social proposals increased 20%.[17] And exempt solicitation filings, which allow activists to advocate for and draw publicity to their proposals, have increased by 70% since 2020.[18] These proposals come from a vanishingly small number of activists—just 10 proponents accounted for more than 60% of all proposals submitted in 2022[19]—yet these individuals' agendas force companies and their shareholders to expend significant resources and court controversy by wading into political topics unrelated to the business.

The SEC is increasingly a partner in these activists' efforts. When a company wishes to exclude a shareholder proposal under Rule 14a-8, it must first seek permission from the SEC through the Division of Corporation Finance's no-action process. In 2022, the success rate for these no-action requests plummeted: from 71% in 2021 to 38% in 2022.[20] In other words, companies are increasingly being forced to include politically motivated proposals on their proxy ballot, at significant expense—a trend that will likely persist as the SEC continues to implement SLB 14L and if it finalizes its proposed amendments to the Rule 14a-8 exclusion criteria.

---

[13] NAM Comments on SLB 14L (30 November 2021). *Available at* https://documents.nam.org/tax/nam_comments_slb_14l.pdf.

[14] *Substantial Implementation, Duplication, and Resubmission of Shareholder Proposals Under Exchange Act Rule 14a-8*, 87 Fed. Reg. 45052 (27 July 2022). Release Nos. 34-95267, IC-34647; *available at* https://www.govinfo.gov/content/pkg/FR-2022-07-27/pdf/2022-15348.pdf.

[15] Rosati, Brigid, Kilian Moote et al., *A Look Back at the 2022 Proxy Season* (23 October 2022). Georgeson LLC. *Available at* https://corpgov.law.harvard.edu/2022/10/23/a-look-back-at-the-2022-proxy-season/.

[16] Copland, James R., *Proxy Monitor 2022 Voting Results: Mid-Season Review* (19 May 2022). Manhattan Institute. *Available at* https://www.manhattan-institute.org/proxy-monitor-2022-mid-season-review.

[17] *Shareholder Proposal Developments During the 2022 Proxy Season* (11 July 2022). Gibson, Dunn & Crutcher LLP. *Available at* https://www.gibsondunn.com/shareholder-proposal-developments-during-the-2022-proxy-season/.

[18] *Ibid.*

[19] *2022 Proxy Season Review: Part 1* (2 August 2022). Sullivan & Cromwell LLP. *Available at* https://www.sullcrom.com/SullivanCromwell/_Assets/PDFs/Memos/sc-publication-2022-Proxy-Season-Part-1-Rule-14a-8.pdf.

[20] Gibson Dunn 2022 Proxy Season Review, *supra* note 17.

This politicization of the proxy ballot is illustrative of the fundamental flaw at the heart of Rule 14a-8: the SEC lacks the statutory authority to require public companies to include shareholder proposals on their proxy ballots. Forcing companies to speak on these policy proposals and to subsidize activists' speech are clear violations of the First Amendment's prohibition on government-compelled speech. Rule 14a-8 outlines the circumstances in which "a company *must* include a shareholder's proposal in its proxy statement,"[21] and the SEC's no-action letters are the definitive authority as to whether a company can exclude a given proposal. Because Rule 14a-8 "plainly alters the content of [companies'] speech," it is "a content-based regulation of speech"[22]—especially given that publishing and speaking on activists' proxy ballot proposals is certainly not "limited to purely factual and uncontroversial information."[23, 24]

The NAM is encouraged that the Subcommittee is considering legislation to block activists and the SEC from politicizing the proxy process. Manufacturers support the following bills, which would keep activists out of the boardroom and enable companies and their shareholders to focus on issues that drive the long-term growth, job creation and innovation critical to America's competitiveness on the world stage and manufacturing workers' lives and careers here at home.

Rule 14a-8(i)(12) Resubmission Thresholds

Under Rule 14a-8, failed shareholder proposals must be included on the following year's proxy ballot if they have achieved a certain level of shareholder support. Proposals receiving as little as 5% support—which is to say, those opposed by 95% of shareholders—are guaranteed a place on a subsequent year's ballot despite overwhelming opposition from the shareholder base. This empowers activists pursuing niche agendas and the proxy advisory firms whose support for these proposals virtually guarantees they will exceed the necessary threshold for resubmission.

The NAM supports draft legislation that would increase the resubmission thresholds to require a more substantial level of shareholder support before allowing a failed proposal back on the proxy ballot. Specifically, to qualify for resubmission, a proposal would have to achieve 10% support if voted on once, 20% support if voted on twice or 40% support if voted on three or more times. These reforms would prevent companies from being forced to include on the proxy ballot proposals that have been rejected by an overwhelming majority of shareholders.

Rule 14a-8(i) Exclusion Criteria

In 2022, the SEC proposed a rule to narrow the exclusion criteria under Rule 14a-8. The SEC's proposed rule would make it more difficult for companies to exclude proposals that have already been substantially implemented, are duplicative of other proposals on a given year's proxy ballot or have been rejected by a large percentage of the shareholder base in previous years.

The NAM supports draft legislation that would block the SEC from finalizing its proposed rule. By preserving the existing exclusion criteria, the bill would make it more difficult for activists to flood the proxy ballot with substantially implemented, duplicative and resubmitted proposals.

---

[21] 17 C.F.R. 240.14a-8 (emphasis added).

[22] *Nat'l Inst. of Fam. & Life Advocs. v. Becerra*, 138 S. Ct. 2361, 2371 (2018).

[23] *Id.* at 2372.

[24] The NAM recently intervened in litigation to show that the SEC's actions dictating the content of public company proxy ballots are unlawful. *See* Mtn. for Leave to Intervene, *National Center for Public Policy Research v. SEC*, No. 23-60230 (5th Cir.).

Exclusion of Politically Motivated Shareholder Proposals

The SEC lacks the statutory authority to force companies to include politically motivated shareholder proposals on their proxy ballots. But under SLB 14L the SEC has adopted the official policy that companies must always include proposals that raise issues of "broad societal impact," even if those issues have no relationship to their operations.

The NAM supports draft legislation that would clarify that companies can always exclude shareholder proposals that seek to advance environmental, social and political agendas unrelated to their business. This change would ensure that the proxy ballot remains focused on issues that are relevant to long-term growth and shareholder value creation.

SLB 14L

Issued in November 2021, SLB 14L rescinded the SEC's content-neutral guardrails that previously had enabled companies and investors to take a company-specific approach to evaluating the relevance and appropriateness of shareholder proposals submitted to company proxy ballots. In place of the rescinded standards, SLB 14L announced that the SEC would "no longer focus on determining the nexus between a policy issue and the company," instead requiring all proposals with a "broad societal impact" to be included on the proxy ballot whenever submitted.

The NAM supports draft legislation that would revoke this damaging policy and allow companies to omit shareholder proposals based on the Rule 14a-8 exclusion criteria, irrespective of whether they relate to a significant social policy issue. SLB 14L has encouraged activists to submit and the SEC to endorse proposals wholly unrelated to long-term value creation, so this change would be a welcome return to a proxy process focused on business growth and investor value.

SEC Authority to Require Inclusion of Shareholder Proposals

The SEC's policy of requiring the inclusion of certain shareholder proposals on public company proxy ballots is a clear violation of the First Amendment's prohibition on government-compelled speech. It is unlawful for the federal government to force companies to speak on these politically motivated proposals and to require them to subsidize activists' speech by publishing proposals in their proxy materials.

The NAM supports draft legislation that would prevent the SEC from compelling companies to include any shareholder proposal on their proxy ballots. In so doing, the bill would protect manufacturers' First Amendment rights and prevent companies and their shareholders from being forced to consider irrelevant and politically motivated proposals on an annual basis.

SEC Study on the Proxy Process

The politicization of the proxy process impacts companies of all sizes, including small businesses. Growing companies often lack the resources to combat activist efforts. They may also be impacted when politically motivated proposals force larger businesses to commit to changes within their value chain that flow down to small and privately held suppliers and customers.

The NAM supports draft legislation that would require the SEC to conduct a comprehensive study on the proxy process. The study would examine the impacts of Rule 14a-8, the role of proxy advisory firms and the costs of politically motivated shareholder proposals. This is critical information necessary for Congress and the SEC to fully understand what changes are necessary to protect companies of all sizes from costly and undue influence.

II. Reining in Proxy Advisory Firms

Proxy advisory firms play a central role in the proxy process by providing voting research, recommendations and other services to institutional investors. Two firms—ISS and Glass Lewis—are estimated to control more than 97% of the proxy advice market. Yet as this duopoly's influence has increased in recent years, due in large part to the increase in institutional ownership of American stocks, the regulatory guardrails under which proxy firms operate have failed to keep pace. Until recently, there has been little-to-no regulation of these powerful entities and minimal accountability for their conflicts of interest, opaque methodologies, rigid and inflexible policies, propensity for errors and misleading statements and unwillingness to engage with publicly traded companies. For example:

- Proxy firms operate with undisclosed and unaddressed conflicts of interest. Of particular concern, ISS operates a consulting business that counsels companies on the very corporate governance policies on which the advisory side of the firm makes recommendations.

- Proxy firms insist upon a one-size-fits-all approach to corporate governance that does not take into account differences in companies' business models and the flexibility allowed under securities law. Increasingly, they also seek to shape rather than analyze and report on corporate behavior, particularly as it relates to ESG issues.

- The guidelines on which proxy firms based their recommendations, and the recommendations themselves, are developed with minimal transparency or stakeholder input. The lack of transparency associated with these quasi-regulatory standards is a significant contrast to the rigorous notice-and-comment procedures that the SEC and other regulators are required to follow.

- Proxy firm reports and recommendations feature a multitude of errors and misleading statements, ranging from specific incorrect facts to mistaken assumptions about, for instance, a company's peer group or compensation practices. The recommendations also feature terms with common market meanings like "total shareholder return" but often use opaque calculation methodologies that vary from traditional market practice.

- Proxy firms have been steadfastly resistant to engaging in a productive dialogue with issuers to correct errors and misunderstandings. Indeed, following the finalization of the SEC's 2020 proxy firm rule, ISS rescinded the limited issuer engagement practices it had previously had in place.

- Proxy firms often engage in the automatic submission of proxy votes on behalf of their clients in a practice known as "robo-voting." Robo-voting deprives asset managers—and by extension the Main Street investors they represent—of an opportunity to review a proxy firm's recommendation and make an informed voting decision.

In 2020, the SEC finalized a long-awaited rule to provide appropriate oversight of proxy advisory firms.[25] The 2020 rule, developed over the course of a decade, instituted commonsense safeguards designed to increase transparency into these powerful actors. In particular, the rule required proxy firms to provide copies of their final recommendations to companies and to have a mechanism in place by which investors could become aware if a company submitted a response to the firm's recommendation. It also required proxy firms to disclose their conflicts of interest and clarified that proxy firms are subject to the proxy solicitation rules' antifraud standards. Alongside the final rule, the

[25] *Exemptions From the Proxy Rules for Proxy Voting Advice*, 85 Fed. Reg. 55082 (3 September 2020). Release No. 34-89372; *available at* https://www.govinfo.gov/content/pkg/FR-2020-09-03/pdf/2020-16337.pdf.

SEC issued guidance to asset managers outlining instances in which relying on proxy firms' robo-voting services instead of reviewing all information available to them and making an informed voting decision could implicate their fiduciary obligations to Main Street investors.[26]

Notably, the 2020 rule's issuer engagement requirements were significantly less strict than what the SEC had proposed in 2019.[27] The 2019 proposal would have required proxy firms to allow companies to review and provide feedback on their *draft* recommendations—a policy idea that dates back to at least the SEC's 2010 Concept Release on the U.S. Proxy System.[28] Proxy firms also would have been required to disseminate company responses to their clients alongside their voting advice. The NAM strongly supported, and continues to support, the draft review and feedback provisions from the 2019 proposal.

Despite the compromise approach adopted by the 2020 rule, in 2021 the SEC's new leadership began to take steps to dismantle this important progress. In a series of actions in June 2021, the SEC announced it would "revisit" the 2020 rule[29] and suspend enforcement of the rule;[30] the SEC also made clear to ISS in a court filing that the decision to suspend enforcement granted proxy firms "relief" from the rule's compliance requirements.[31] In a lawsuit brought by the NAM, a federal judge found that this suspension of the rule, which was effectuated absent the notice-and-comment proceedings required by the Administrative Procedure Act, was unlawful.[32]

In November 2021, the SEC proposed a rule to rescind critical provisions of the 2020 rule, including the compromise requirement that proxy firms share their recommendations with impacted companies after they are finalized and take steps to ensure that investors have access to any company responses to those recommendations.[33] The rescission, which manufacturers strongly opposed,[34] was finalized in July 2022.[35] Concomitant with the rescission of the 2020 rule, the SEC also rescinded the 2020 robo-voting guidance.

---

[26] *Supplement to Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers*, 85 Fed. Reg. 55155 (3 September 2020). Release No. IA-5547; *available at* https://www.govinfo.gov/content/pkg/FR-2020-09-03/pdf/2020-16338.pdf.

[27] *See Amendments to Exemptions From the Proxy Rules for Proxy Voting Advice*, 84 Fed. Reg. 66518 (4 December 2019). Release No. 34-87457; *available at* https://www.govinfo.gov/content/pkg/FR-2019-12-04/pdf/2019-24475.pdf.

[28] *See Concept Release on the U.S. Proxy System*, 75 Fed. Reg. 42982 (22 July 2010). Release Nos. 34-62495; IA-3052; IC-29340, *available at* https://www.govinfo.gov/content/pkg/FR-2010-07-22/pdf/2010-17615.pdf. For instance, the Concept Release observes that proxy firms "may be unwilling, as a matter of policy, to accept any attempted communication from the issuer or to reconsider recommendations in light of such communications" and notes that "issuers have expressed a desire to be involved in reviewing a draft of the proxy advisory firm's report, if only for the limited purpose of ensuring that the voting recommendations are based on accurate issuer data" (at 43012).

[29] *Statement on the Application of the Proxy Rules to Proxy Voting Advice* (1 June 2021). Chairman Gary Gensler. *Available at* https://www.sec.gov/news/public-statement/gensler-proxy-2021-06-01.

[30] *Statement on Compliance with the Commission's 2019 Interpretation and Guidance Regarding the Applicability of the Proxy Rules to Proxy Voting Advice and Amended Rules 14a-1(1), 14a-2(b), 14a-9.* SEC Division of Corporation Finance (1 June 2021). *Available at* https://www.sec.gov/news/public-statement/corp-fin-proxy-rules-2021-06-01.

[31] *See* Mtn. for Abeyance, *Institutional Shareholder Services Inc. v. SEC*, No. 19-cv-3275 (D.D.C.). The NAM is an intervenor-defendant in this case.

[32] *See Nat'l Ass'n of Mfrs. v. SEC*, 2022 WL 16727731 (W.D. Tex. 2022).

[33] *Proxy Voting Advice*, 86 Fed. Reg. 67383 (26 November 2021). Release No. 34-93595; *available at* https://www.govinfo.gov/content/pkg/FR-2021-11-26/pdf/2021-25420.pdf.

[34] NAM Comments on Proxy Firm Rescission Rule (24 December 2021). *Available at* https://documents.nam.org/tax/nam_proxy_comments_2021.pdf.

[35] *Proxy Voting Advice*, 87 Fed. Reg 43168 (19 July 2022). Release Nos. 34-95266, IA-6068; *available at* https://www.govinfo.gov/content/pkg/FR-2022-07-19/pdf/2022-15311.pdf.

The rescission was effectuated via an abbreviated notice-and-comment process that SEC Commissioner Mark Uyeda described as a "regulatory seesaw" that "does not reflect administrative 'best practices' that promote long term reliance and confidence by market participants in the stability of important areas of securities regulation."[36] At no point during this truncated rulemaking did the SEC provide any reasonable justification for why the same record that supported the 2020 rule two years prior suddenly required its rescission, in clear violation of the APA.[37]

Given proxy firms' continued outsized influence on corporate governance at manufacturers of all sizes—and the SEC's ongoing efforts to deregulate these powerful actors—congressional action is clearly needed. The NAM appreciates that the Subcommittee is considering legislation to rein in proxy advisory firms. Manufacturers support the following bills, which would address proxy firms' significant conflicts of interest and minimal accountability and transparency.

Proxy Firm Registration

Given the SEC's rescission of much of its 2020 proxy firm rule, more must be done to provide appropriate regulatory oversight of proxy firms. In particular, the NAM supports efforts to require proxy firms to offer companies an opportunity to review and provide feedback on draft recommendations, ensure that investors have access to company responses and prevent proxy firms from distorting company decisions and investor votes by offering consulting services to the same companies whose governance is the subject of their voting advice.

The NAM supports draft legislation, sponsored by Rep. Bryan Steil (R-WI), that would require proxy firms to register with the SEC. As a condition of registration, proxy firms would be required to:

- Provide companies with the data and information underpinning their recommendations, and grant companies an opportunity to share feedback to correct errors and misrepresentations;
- Employ an ombudsman charged with engaging with companies and resolving issues identified by impacted businesses;
- Include any company statements responding to the firm's recommendations in its final report to clients;
- Certify that the firm has sufficient staff and resources to provide voting advice based on accurate information and in the economic best interests of shareholders;
- Provide disclosures on the firm's procedures, methodologies, organizational structure, professional qualifications and code of ethics; and
- Adopt policies to identify, disclose and manage any conflicts of interest.

Additionally, proxy firms would be prohibited from providing advisory or consulting services that present a conflict of interest with respect to their recommendations.

These reforms will improve the quality, accuracy and reliability of proxy voting advice, and they are essential to countering the threat that proxy firms' outsized influence poses to everyday Americans' retirement savings. The NAM applauds Rep. Steil for his years of leadership on this critical issue, and manufacturers strongly support his draft legislation to bring appropriate oversight to the proxy advice industry.

---

[36] *Statement on Final Rule Amendments on Proxy Voting Advice* (13 July 2022). Commissioner Mark Uyeda. *Available at* https://www.sec.gov/news/statement/uyeda-statement-amendments-proxy-voting-advice-071322.

[37] The NAM's lawsuit challenging the rescission as unlawful under the APA is currently pending before the Fifth Circuit Court of Appeals. *See Nat'l Ass'n of Mfrs. v. SEC,* No. 7:22-cv-163-DC (5th Cir.).

Proxy Firm Antifraud Liability

The 2020 proxy firm rule clarified that proxy voting advice constitutes a solicitation under the Exchange Act, subjecting proxy firms to the proxy solicitation rules, including those rules' antifraud standards. Specifically, the 2020 rule noted that proxy firms may need to provide appropriate disclosures with respect to their methodologies, sources of information and conflicts of interest in order to ensure that their advice is not false or misleading.

In rescinding much of the 2020 rule, the SEC in 2022 removed the language that had been added to the antifraud standards about proxy firms' methodologies, sources of information and conflicts of interest. While proxy firms are still subject to antifraud liability under the rescission, the standards under which that liability may apply have been significantly weakened.

The NAM supports draft legislation, sponsored by Rep. Steil, that would clarify that the failure to disclose material information associated with proxy voting advice, such as information about a proxy firm's methodologies, sources of information and conflicts of interest, would render the advice false or misleading. This change is critical to ensuring that proxy firm clients have access to the material information they need to make fully informed voting decisions.

III. Protecting Main Street Investors

Most Americans' primary exposure to the stock market is through passive investing vehicles like mutual funds, pension plans and 401(k) accounts. These funds allow Main Street investors to share in manufacturing's success and set the stage for financial security for American families. The day-to-day operations of these funds, including asset allocation and proxy voting, are overseen by fund or plan managers employed by large institutional investors. These institutions have a fiduciary duty to the underlying beneficial owner of the securities the fund holds: everyday Americans saving for a new home, a child's education or a secure retirement. Fund managers are legally obligated to act in these investors' financial best interests.

As public company governance has become increasingly politicized in recent years, questions have arisen about the proper role and responsibilities of the asset managers charged with protecting Main Street investors' holdings. Many institutional investors over-rely on the recommendations of proxy advisory firms, for example. A 2018 study found that 175 institutions, with more than $5 trillion in assets under management, voted in lock step with proxy firms more than 95% of the time.[38] This outsourcing of important proxy voting decisions has been further enabled by the SEC's rescission of its 2020 robo-voting guidance.

More broadly, some asset managers may be prioritizing goals unrelated to shareholder value creation by making asset allocation and proxy voting decisions based on ESG criteria, and many Main Street investors are unaware that these decisions could increase their risks or reduce their returns. For example, many asset managers allocate funds or cast proxy votes based on grades published by ESG ratings organizations, despite these groups' lack of transparency, consistency or engagement with companies—and their stated goal of achieving social policy outcomes rather than enhancing shareholder value.

The NAM is encouraged that the Subcommittee is considering legislation to ensure that Wall Street fund managers are acting in the best interests of manufacturing workers and other Main Street investors. Manufacturers support the following bills, which would limit robo-voting, prevent asset

[38] Doyle, Timothy M., *The Realities of Robo-Voting* (9 November 2018). American Council for Capital Formation. *Available at* https://accfcorpgov.org/wp-content/uploads/ACCF-RoboVoting-Report_11_8_FINAL.pdf.

managers from over-relying on proxy firms and protect the long-term financial best interests of everyday Americans.

Asset Manager Reliance on Proxy Firm Recommendations

Despite their fiduciary duty to Main Street investors and retirees, some asset managers are over-relying on the ratings and recommendations of proxy firms and ESG ratings organizations and may be making proxy voting decisions based on criteria divorced from shareholders' financial best interests.

The NAM supports draft legislation that would require investment advisers, asset managers and pension funds relying on the services of a proxy firm to explain how the firm's recommendations impacted their proxy votes, analyze their voting decisions based on investors' economic best interests and the institution's fiduciary duty and disclose the degree to which the institution voted in line with the firm's recommendations. These institutions would also be required to certify that their voting decisions were made based solely on the economic best interests of their customers and beneficiaries.

These safeguards would ensure that the institutions charged with protecting Main Street investors' retirement security are acting in those investors' best interests. They would also give everyday Americans the information they need to make decisions about how their savings are managed.

Robo-Voting

Robo-voting allows proxy firms to automatically cast votes on their clients' behalf—in line with the proxy firm's recommendations and without any review by the asset manager. As former SEC Commissioner Elad Roisman has noted, these "set-it-and-forget-it" mechanisms are generally not well understood by the investors whose shares are being voted, nor are they always consistent with an investment adviser's fiduciary duties.[39]

The NAM supports draft legislation that would prevent institutional investors from outsourcing proxy voting decisions to proxy advisory firms via the firms' robo-voting services. This prohibition on robo-voting would ensure that asset managers actually review the information available to them before casting proxy votes that could impact the direction of a business and the performance of everyday Americans' investments.

Proxy Voting by Passively Managed Funds

Many Americans participate in passively managed funds, which are designed to track a certain set of companies within an industry or the economy writ large. For example, most institutions offer a version of an S&P 500 fund, which simply holds shares proportionally of every company in the S&P 500 index. As new companies are added to or dropped from the index, or their relative size increases or decreases, the fund will make asset allocation changes accordingly. The managers of these funds do not exercise any independent judgment with respect to its holdings; they simply track the index. But, in some cases, these *passive* managers have taken an *active* role in companies' corporate governance by leveraging the fund's holdings via proxy votes.

The NAM supports draft legislation that would require managers of passive funds to stay passive—which is to say, to defer to the judgment of companies' boards of directors and to rely on those directors' fiduciary duty to shareholders. Unless instructed otherwise by their clients, passive funds

[39] *Speech at the Council of Institutional Investors' Conference* (10 March 2020). Commissioner Elad L. Roisman. *Available at* https://www.sec.gov/news/speech/speech-roisman-cii-2020-03-10.

would be required to vote in alignment with a company's voting recommendations on most proxy ballot measures, with exceptions for issues like director elections and executive compensation. Passive funds could also choose to abstain from voting. These reforms would ensure that fund managers are appropriately representing the Main Street investors who have chosen to participate in a passive fund.

IV. Limiting ESG Disclosure Mandates

Over the past two years, the SEC has expanded its regulatory ambit into policy areas not traditionally subject to Commission action. In particular, the SEC's focus on ESG issues has undermined the long-settled materiality standard governing public company disclosure obligations. This departure from materiality has in many instances led to disclosure requirements justified solely by policy concerns outside the SEC's purview, a concerning trend for an agency whose disclosure rules should be designed to protect investors and facilitate capital formation.

The SEC is legally constrained by the confines of its statutory authority,[40] and that authority is centered on facilitating the provision of material information for the protection of investors. As recently as 2016, the SEC itself made clear that "disclosure relating to environmental and other matters of social concern should not be required of all registrants unless appropriate to further a specific congressional mandate or unless, under the particular facts and circumstances, such matters are material."[41] To the extent that the SEC's proposed ESG reporting requirements exceed material disclosures necessary for a reasonable investor to understand the total mix of information available about an issuer and to make a corresponding investing decision, they are unlawful.[42]

For instance, in March 2022 the SEC proposed a novel, one-size-fits-all climate reporting mandate that would impose tremendous costs on all public companies, as well as on the private businesses within their supply chains.[43] Manufacturers are dedicated to combatting climate change and to providing appropriate disclosures about these efforts, but the SEC's proposed rule would require reporting far in excess of the material information necessary for investors to make informed decisions. In response to the proposed rule, the NAM expressed concern that it would "institute[ ] a wide-ranging mandate for public companies to generate and report pages upon pages of information, much of which is not material to their operations or financial performance," ultimately resulting in "substantially increase[d] compliance costs and legal risks for public companies—despite limited investor benefit."[44]

A centerpiece of the proposed climate disclosures rule is its mandate that public companies report their so-called "Scope 3" emissions: those attributable to the suppliers and customers within their value chains. This requirement will expose public companies, as well as a wide range of small and

---

[40] *See, e.g., Global Tel*Link v. FCC*, 866 F.3d 397, 412 (D.C. Cir. 2017) (vacating an FCC regulation as "beyond the statutory authority of the Commission" where the agency acted to further a "desirable social policy" while ignoring statutory limits).

[41] *Business and Financial Disclosure Required by Regulation S-K*, 81 Fed. Reg. 23916 (22 April 2016). Release Nos. 33-10064, 34-77599; *available at* https://www.govinfo.gov/content/pkg/FR-2016-04-22/pdf/2016-09056.pdf.

[42] *See Utility Air Regulatory Grp. v. EPA*, 573 U.S. 302, 314–316 (2014) (noting that courts routinely hold unlawful agency action in violation of statutory limits on agencies' authority); *see also Reuters Ltd. v. FCC*, 781 F.2d 946, 95 (D.C. Cir. 1986) (explaining that an agency may not "deviate from its rules in order to achieve what it deems to be justice").

[43] *The Enhancement and Standardization of Climate-Related Disclosures for Investors*, 87 Fed. Reg. 21334 (11 April 2022). Release Nos. 33-11042, 33-94478; *available at* https://www.govinfo.gov/content/pkg/FR-2022-04-11/pdf/2022-06342.pdf.

[44] NAM Comments on Proposed Climate Disclosures Rule (6 June 2022). *Available at* https://documents.nam.org/tax/nam_comments_sec_climate_rule.pdf.

privately held businesses, to a costly reporting burden that in many instances will prove infeasible or impossible given the uncertain nature of Scope 3 tracking and estimation methodologies. But Scope 3 emissions data is unlikely to be material to a shareholder's investing decisions, especially as Scope 3 reporting methodologies continue to evolve. Lacking a robust link to shareholder value creation, the Scope 3 mandate, like many other provisions in the climate rule, represents the SEC pursuing substantive outcomes with respect to major questions about climate policy.

The climate rule is just one example of the SEC's regulatory overreach. Other rulemakings, such as the proposed cybersecurity disclosures rule and the recently finalized stock buybacks disclosures rule, similarly impose immaterial disclosure mandates on public companies. And the SEC has announced that it plans to propose a human capital management rule later this year, replacing the Commission's existing human capital reporting requirement—which requires disclosure only of material human capital measures or objectives—with something more expansive. These new mandates are illustrative of the costly and burdensome regulatory onslaught manufacturers are currently experiencing at the hands of the federal government.

International financial regulators are also taking steps to increase corporate disclosure obligations beyond the material information that investors need. The European Union's Corporate Sustainability Reporting Directive is based on the concept of "double materiality," requiring disclosure of information necessary to understand a business's sustainability impact, not its financial performance. And the EU's Corporate Sustainability Due Diligence Directive would go even further, requiring companies to take steps to identify and mitigate certain environmental and social impacts throughout their value chains.

The NAM appreciates that the Subcommittee is considering legislation to rein in this onslaught and block ESG disclosure mandates that require reporting beyond material information. Manufacturers support the following bills, which would prevent regulators from increasing costs and liability for manufacturers and overwhelming investors with a deluge of irrelevant information.

Mandatory Materiality Requirement Act

The Supreme Court has held that information is only material if there is a "substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[45] Investors are not unanimous in what, if any, climate and ESG metrics they would like to see from public companies, so the materiality standard's emphasis on the *reasonable* investor focuses public company disclosures on metrics that actually drive value creation and long-term shareholder return. Unfortunately, the SEC's proposed ESG mandates would require disclosures in excess of this time-tested and well-understood standard.

The NAM supports the Mandatory Materiality Requirement Act, which would allow the SEC to require disclosure only of information that is material to a shareholder's voting or investment decision pursuant to the Supreme Court's materiality definition. Limiting the SEC's authority to mandate immaterial disclosures would reduce costs for public companies while also ensuring that their reports are useful to investors.

SEC Justification of Non-Material Disclosure Requirements

The SEC's regulatory onslaught has resulted in disclosure obligations for public companies that are not grounded in materiality. The NAM supports draft legislation that would require the SEC to maintain a list of non-material disclosure requirements and provide a justification for why each

[45] *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438 (1976); *see also Basic, Inc. vs. Levinson*, 485 U.S. 224 (1988).

disclosure is necessary. It would also clarify that a company choosing not to disclose non-material information would not be subject to a private right of action. These reforms would limit non-material disclosure obligations and protect companies from the increased liability that often flows from such requirements.

* * * *

On behalf of the NAM and the millions of people who make things in America, I appreciate the opportunity to testify before the Subcommittee today. Congressional action is needed to institute appropriate guardrails for the proxy process that will counter the SEC's regulatory overreach and depoliticize the business decisions that impact the lives and life savings of millions of Americans. The NAM looks forward to working with the Subcommittee to advance policies that preserve the public market as an avenue to capital formation for manufacturers—allowing our industry to create jobs, lead the economy and improve the quality of life for all Americans.

HEARING BEFORE THE SUBCOMMITTEE ON CAPITAL MARKETS OF THE COMMITTEE ON FINANCIAL SERVICES OF THE UNITED STATES HOUSE OF REPRESENTATIVES

Reforming the Proxy Process to Safeguard Investor Interests

Testimony of Dr. Joshua T. White
July 13, 2023

Chairwoman Wagner, Ranking Member Sherman and members of the Subcommittee on Capital Markets: Thank you for inviting me today to appear to discuss critical reforms to the proxy process to safeguard investor interests. I am an Assistant Professor of Finance and the Brownlee O. Currey Jr. Dean's Faculty Fellow at Vanderbilt University's Owen Graduate School of Management. I have been a tenure-track faculty member since 2017. Over 2012 to 2018, I served as a financial economist and expert consultant in the Division of Economic and Risk Analysis at the U.S. Securities and Exchange Commission (SEC).

1. General Description of Proxy Voting

Currently, the House Financial Services Committee is considering several legislative proposals aimed at overhauling the proxy process and protecting the interests of investors. Investor-related issues are paramount for ordinary Americans who put their hard-earned money into public equities to achieve financial objectives. These goals often include home purchase savings, funding their children's college education, or creating a retirement savings capable of keeping pace with inflationary trends.

The procedure of proxy voting holds an incredible significance for investors. This importance is embodied by the way I structure my corporate financial policy classes at Vanderbilt. I start each new MBA course by emphasizing the crucial role that the proxy process plays in corporate governance by allowing shareholders to vote on director nominees and issues that are critical to an issuer's long-term value creation.

Shareholder relinquish day-to-day business operation decisions to managers, who are overseen by a board of directors who are fiduciaries for the shareholders. Shareholders principal means of oversight over the board of directors is through the voting process. Thus, shareholder voting rights are critically important to investor protection.

Shareholders exercise their voting rights at annual or special meetings. Annual meetings enable voting on an array of matters, including director appointments, auditor ratification, proposals related to governance modifications; and non-binding advisory votes on executive compensation or proposals sponsored by shareholders. Prior to annual meetings, issuers deliver proxy materials to shareholders. These documents detail the resolutions to be voted on and are accompanied by board recommendations on voting.

Today, I will address three current issues vital for safeguarding investor interests. First, I will discuss the rising trend of a multitude of shareholder proposals, commonly known as ESG (Environmental, Social, and Governance) initiatives. I will discuss how the quantity of E&S proposals by special interest groups has surged while shareholder support has plummeted. I will present data that demonstrates that this trend is largely due to changes in SEC Staff Guidance made in 2021 and that the costs are ultimately borne by all investors. Second, I will outline the role of proxy advisory firms and their impact on investor returns and corporate conduct that are inconsistent with shareholder value maximization. Third, I will highlight the trend of the SEC introducing rules that mandate non-material E&S information disclosure and its expected consequences. If these compliance costs are not offset by information benefits, it can deter companies from going public, ultimately restricting retail investors' investment opportunities.

2. Shareholder Proposals

2.1. SEC Staff Fundamentally Altered the Shareholder Proposal Process in 2021

Rule 14a-8 of the Securities Exchange Act of 1934 sets the guidelines for including shareholder proposals at annual or special meetings. This rule lists the reasons that an issuer may exclude a shareholder proposal from being voted upon. When a shareholder introduces a proposal, managers can: 1) put the proposal on the proxy for a vote at the meeting; 2) engage in negotiations with the proposal's sponsor to facilitate its withdrawal; or 3) request a no-action relief from the SEC under specific paragraphs of Rule 14a-8, which would allow them to exclude the proposal if granted.

Historically, the most frequent reasons for exclusion under Rule 14a-8 are for proposals that deal with ordinary business operations (paragraph (i)7); and for proposals that are already substantially implemented (paragraph (i)10) (Burke, 2023). These reasons for exclusion represent 34% and 26% of granted no-action relief by the SEC, respectively, based on data downloaded from the ISS Voting Analytics database over 2018 to 2022. Stock prices tend to respond positively to the announcement of a no-action relief by the SEC, indicating that managers typically challenge the proposals that have the potential to destroy value (Matsusaka, Ozbas, and Yi, 2021; Burke, 2023).

The SEC staff regularly offers interpretative guidance that summarizes or elucidates adopted or amended rules. In the context of Rule 14a-8, this guidance sets an informal precedent and aids participants in estimating probable outcomes of no-action relief requests for proposals. By offering and following clear guidance, SEC staff can reduce uncertainty, and consequently save time and costs for managers and shareholders, as well as the SEC.

In November 2021, the SEC staff rescinded its prior guidance and amended its longstanding position on how it would treat requests for no-action relief under Rule 14a-8. In Staff Legal Bulletin No. 14L ("SLB 14L"), the SEC staff revised its interpretations of Rule 14a-8 to limit the ability of issuers to receive relief for proposals with significant social policy implications. The new guidance reduced the predictability of no-action relief requests, thereby complicating the decision-making process for managers wishing to exclude shareholder proposals and for shareholders wishing to sponsor them.

According to information shared by SEC Commissioner Mark Uyeda, before the release of SLB 14L, the SEC staff disagreed with requests to omit proposals for ordinary business operations under paragraph i(7) 25% of the time. However, after SLB 14L's issuance, the staff disagreement rate with i(7) surged to 54%. These data demonstrate a similar pattern for requests to exclude proposals that issuers argued were substantially implemented under (i)(10) (Uyeda, 2023).

The decline in no-action relief suggests that the issuance of SLB 14L transformed the shareholder proposal process. In July 2022, the SEC proposed changes to exclusion parameters for shareholder proposals as defined in paragraphs (i)(10), (i)(11), and (i)(12), which concern substantial implementation, duplication, and resubmissions respectively (SEC, 2022). Although these changes have not been adopted, if we consider the trends post-SLB 14L, we could anticipate that these finalized rules might further intensify the challenge for managers to exclude shareholder proposals that they view as value destroying.

2.2. E&S Shareholder Proposals Proliferated after SLB 14L but with Less Shareholder Support

The alterations brought about by SLB 14L align with a notable increase in shareholder proposals that failed to be excluded and were ultimately presented for a shareholder vote. This surge in shareholder proposals is primarily focused on Environmental and Social ("E&S") aspects, rather than Governance ("G") factors based on data discussed below and figures presented in the Data Appendix. The support for these E&S proposals drops precipitously. Taken together, these two facts suggest that SLB 14L likely resulted in an overload of E&S proposals that shareholders perceive as not beneficial, or even detrimental, to long-term value.

2.2.1. Shareholder Proposals Voted Upon

Figure 1 illustrates the annual count of shareholder proposals voted upon from 2018 to 2022 for issuers that are members of the S&P500 index. The data were sourced from the ISS Voting Analytics database and divided into two categories, E&S (black bars) and G (gray bars), according to ISS's resolution type coding. This figure excludes proposals that were initially submitted but later withdrawn or omitted following the SEC's no-action relief.

The graph indicates that, while the volume of governance shareholder proposals voted upon was nearly double that of E&S proposals, they followed similar patterns versus E&S proposals up to 2021, just before SLB 14L. However, in the year following SLB 14L, voted E&S proposals voted upon surge by 100%, jumping from 131 in 2021 to 262 in 2022. Meanwhile, the count of governance proposals remained relatively unchanged.

- The key insight from Figure 1 is that SLB likely had a significant impact on the number of E&S proposals voted upon by shareholders.

2.2.2. Voting Support for Shareholder Proposals

In Figure 2, I present the voting support for shareholder proposals from 2018 to 2022 for S&P500 companies using the same database. I define voting support as the median ratio of votes for to the sum of votes for and against, excluding abstentions. Until 2021, voting support for both governance and E&S proposals follows a consistent pattern, with governance proposals obtaining support in the range of 31-35%, and E&S proposals receiving between 27-34% support. However, these similarities diverge in 2022. Governance proposals maintain their slight upward trend, with an increase in voting support by 1% in 2022. This pattern is consistent with shareholders viewing some of the G proposals as potentially enhancing governance and possibly reducing managerial entrenchment. Yet, E&S proposals exhibit a 32% drop in the voting support.

- The main conclusion from Figure 2 is that shareholders show reduced support for the flood of E&S proposals voted upon after SLB 14L.

2.2.3. Submitted Shareholder Proposals

Figure 3 presents the yearly count of submitted shareholder proposals from calendar year 2018 to 2022 for companies that are members of the S&P500 index. This figure encompasses all proposals, including those that were voted upon, withdrawn, or omitted due to a No-Action Letter from the

SEC. From 2018 to 2020, the volume of E&S and G submitted proposals followed similar patterns and levels. However, there was a 39% surge in E&S submitted proposals in 2021, increasing from 283 to 392. Interestingly, this increase predates SLB 14L, thus the deviation from the previously similar trend occurred prior to SLB 14L in terms of submitted proposals. The surge of E&S proposals persisted into 2022, with an additional increase of 24% to 486. Yet, the count of governance proposals saw an 18% decrease. When combined with the findings in Figure 1, this graph indicates that special interest groups increased the volume of E&S proposals *prior* to SLB 14L, but many of these proposals were excluded until *after* SLB 14L.

- The key takeaway from Figure 3 is that the increase in submitted E&S shareholder proposals slightly pre-dates SLB 14L but further increases after the revised staff guidance.

Recent analysis by Gerber and Adams (2023) shows that, after the high rate of SEC staff disagreements in 2022, issuers submitted fewer requests for no-action exclusions in 2023. The downturn in no-action requests in 2023 suggests that managers and proposal sponsors assume that the SEC is less likely to provide no-action relief for most E&S proposals after SLB 14L.

2.3. Shareholder Proposals are Costly Even if they Receive Low Support

Shareholder proposals impose direct and indirect costs. Direct costs relate to legal fees, which the SEC estimates at up to $150,000 for a single proposal (SEC, 2020). However, the more substantial cost is likely indirect: the unproductive use of time by boards and management. This cost includes the time required to thoroughly evaluate each proposal, formulate a recommendation, and draft an informed response in the proxy statement. Any time spent on a proposal that does not add value is a misallocation of scarce resources. Thus, the current upward trend in unsupported E&S proposals is concerning as it allows special interest groups to burden management with a significant cost that are ultimately borne by all investors, including retail.

Beyond the direct legal costs and time investment, inundating shareholders with proposals can obscure crucial voting decisions. Take Amazon's 2023 proxy statement as an example, where shareholders faced 18 proposals (Amazon, 2023). These proposals and the board's responses took up 61 pages and nearly 40,000 words, over half of the 116-page proxy statement. The proposals primarily addressed E&S aspects of ESG, ranging from the carbon intensity of companies in the default employee retirement plans to the use of facial recognition technology and content removal policies. All 18 proposals failed to gain majority shareholder support. Thus, most investors believed that these proposals would either not impact or harm long-term shareholder value in Amazon's stock. Allowing almost all E&S proposals on a proxy card likely engulfs investors with voting matters and results in less informed voting on other critical issues, especially for widely diversified retail investors who have limited time and resources to investigate them.

3. Proxy Advisory Firms

3.1. Proxy Advisory Firms Provide Fee-Based Voting Recommendations

Proxy advisory firms conduct research on issuers and provide fee-based voting recommendations to institutional investors. Over 75% of annual meetings occur within the months of March, April, and May. By analyzing extensive data on director nominations and proposals, proxy advisors can

help institutional investors lower their fiduciary costs of making informed voting decisions. This cost reduction could be particularly beneficial for passive portfolio managers who typically manage vast portfolios comprising hundreds or even thousands of issuers, thereby reducing their costs of reviewing tens of thousands of pages of proxy statements each year. However, as discussed below, some institutional investors blindly follow proxy advisor recommendations, likely to satisfy fiduciary duties at a low cost. Such "robo-voting" could be problematic as proxy advisory recommendations do not always maximize shareholder value.

3.2. Proxy Advisors have an Outsized Influence on Shareholder Value due to Market Power and Robo-Voting

Voting advice that does not benefit all shareholders is concerning because proxy advisory firms' recommendations are highly influential. Extensive academic research demonstrates that voting recommendations by proxy advisory firms significantly and causally influence large changes in voting outcomes (Malenko and Shen, 2016). One reason for their strong influence is that two advisory firms, Institutional Shareholder Services (ISS) and Glass Lewis, control more than 90% of the market share for advisory services. Thus, institutional investors have few alternatives for outside voting advice.

Another factor contributing to the sway of proxy advisory firms is the propensity of asset managers to resort to robo-voting, which involves aligning with nearly all voting recommendations provided by a proxy advisory firm. One study uncovered that 175 institutional investors, who collectively manage over $5 trillion in assets, voted in accordance with Institutional Shareholder Services (ISS) recommendations more than 95% of the time (Doyle, 2018). Other studies indicate that almost a quarter of mutual funds heavily rely on ISS recommendations, and these funds often underperform, yielding lower shareholder returns (Iliev and Lowry, 2015). This evidence suggests that robo-voting could potentially impair shareholder value, and that the advice provided by proxy advisory firms does not always align with preserving shareholder interests.

3.3. Proxy Advisory Recommendations do not Always Maximize Shareholder Value

The net effect of proxy advisory firms' voting advice is highly dependent on the quality of its recommendations (Malenko and Malenko, 2019). Several studies identify how proxy advisory research can harm shareholder value due to standardization of pay plans, a one-size fits all approach to voting advice, reductions in independent information acquisition, and conflicts of interest (Larcker, McCall, and Ormazabal, 2015; Li, 2018; Cabezon, 2022; Malenko et al., 2022).

Research also indicates that some proxy advisors may skew their recommendations on E&S proposals due to pressure from funds focused on socially responsible investment (Matsusaka and Shu, 2022). These asset managers and pension funds often prioritize social objectives like environmental conservation over maximizing shareholder value, which can detrimentally affect shareholder returns (Woidtke, 2002; Riedl and Smeets, 2017). By pressuring proxy advisory firms to support E&S proposals, these funds aim to gain backing from institutional investors that automatically vote following all advice from proxy advisors (Matsusaka and Shu, 2022), a process known as "robo-voting."

3.4. Managers Might Adopt E&S Proposals to Avoid Negative Proxy Advisory Firm Recommendations

Shareholder proposals are advisory and non-binding. However, managers might opt to implement a costly non-binding proposal to avoid losing support from proxy advisory firms. These firms have established policies whereby if a shareholder proposal garners majority support, they anticipate issuers to disclose outreach efforts by the board and whether they enacted the proposal. Even if the proposal does not gain majority backing, directors might still implement proposals that do not increase shareholder value to sidestep negative recommendations against their board appointment from proxy advisors. In the context of other advisory votes, studies illustrate that the policies of ISS prompt directors to engage shareholders when non-binding votes on remuneration fail to receive 70% support, even if the vote receives majority approval (Dey, Starkweather, and White, 2023).

4. Trends in SEC Rule Rulemaking

4.1. Recent SEC Proposed Rules Mandate Disclosures that are Likely Non-Material to Most Investors

In addition to a rise in potential value-destroying E&S proposals, the SEC recently proposed climate related disclosures that some commentators argue would include non-material information (e.g., Lewis and Kothari, 2022). These commentators note that proposed changes in the disclosure requirements represent a significant shift away from the established materiality standard that underpins financial statements. Academic scholarship argues that "materiality forms the conceptual bedrock of corporate reporting." (Eccles and Youmans, 2016). Relying on materiality provided issuers with clear, principles-based operational guidance that removed the burden of supplying expensive overproduction of information that did not benefit shareholders.

4.2. Overly Burdensome Compliance Costs have a Negative Effect on Issuers and Investors

The mounting prevalence of non-value adding E&S proposals, alongside escalating compliance costs due to non-material disclosure mandates, places a substantial burden on public issuers. These costs deter companies from either entering or remaining in the public sphere, thereby negatively influencing investors, impeding job creation, and diminishing the allure of U.S. capital markets.

The journey to becoming, or remaining, a public company carries substantial administrative, legal, and reporting expenses. Heightened compliance obligations magnify these costs, and for smaller firms or startups, this burden can be overwhelming (Lewis and White, 2023). Consequently, these firms may opt to stay private or, if already public, contemplate delisting or merging to reduce these costs (Leuz, Triantis, and Wang, 2008).

A decrease in the number of public companies limits diversification and investment opportunities for investors, particularly retail investors who often have restricted access to private equity markets. The more limited set of investment opportunities curtails retail investors' potential for wealth generation through equity ownership.

Elevated compliance costs could also diminish the appeal of U.S. capital markets. Companies around the world might prefer to list in regions with less burdensome regulations. This change could adversely impact the liquidity, size, and overall competitiveness of U.S. capital markets.

Conclusion

In closing, I believe there are pressing issues in proxy voting that are essential for the protection of investor interests. First is the growing trend of environmental and social shareholder proposals. The proliferation of these proposals by special interest groups has intensified while shareholder support has drastically declined. My analysis indicates that this trend largely results from changes in SEC Staff Guidance towards no-action relief implemented in 2021, with the costs ultimately falling on all shareholders, including retail investors.

Second, the substantial influence of proxy advisory firms on asset manager voting and corporate behavior can sometimes deviate from maximizing shareholder value. Proxy advisory firms have a large influence on voting outcomes due to concentration of market power and the propensity for some institutional investors to predominately follow all their voting recommendations.

Third, I note that the SEC is considering implementing E&S-based rules that many argue would require non-material information disclosure. The repercussions of this such mandates could impact companies deciding whether to go or remain public, the cost of capital formation, and the scope of retail investment opportunities.

References

Amazon.com. (2023, April 13). 2023 annual meeting of shareholders & proxy statement. https://www.sec.gov/ix?doc=/Archives/edgar/data/1018724/000110465923044708/tm233694d2_def14a.htm

Burke, G. (2023). SEC Rule 14a-8 shareholder proposals: No-action requests, determinants, and the role of SEC staff. *Journal of Accounting and Public Policy*, 42, 107048.

Cabezon, F. (2022). Executive compensation: The trend toward one size fits all. Working paper, Virginia Tech University. https://ssrn.com/abstract=3727623

Dey, A., Starkweather, A., White, J. (2023). Proxy advisory firms and corporate shareholder engagement. Harvard Business School WP No. 21-137. https://ssrn.com/abstract=3871948

Doyle, T. (2018, Nov. 29). The realities of robo-voting. *Harvard Law School Forum on Corporate Governance*. https://corpgov.law.harvard.edu/2018/11/29/the-realities-of-robo-voting/

Eccles, R., Youmans, T. (2016). Materiality in corporate governance: The statement of significant audiences and materiality. *Journal of Applied Corporate Finance*, 28, 39-46.

Gerber, M., Adams, R. (2023, Jul. 8). Shareholder proposal no-action requests in the 2023 proxy season. *Harvard Law School Forum on Corporate Governance*. https://corpgov.law.harvard.edu/2023/07/08/shareholder-proposal-no-action-requests-in-the-2023-proxy-season/

Iliev, P., Lowry, M. (2015). Are mutual funds active voters? *Review of Financial Studies*, 28, 446-485.

Larcker, D., McCall, A., Ormazabal, G. (2015). Outsourcing shareholder voting to proxy advisory firms. *Journal of Law and Economics*, 58, 173-204.

Leuz, C., Triantis, A., Wang, T. (2008). Why do firms go dark? Causes and economic consequences of voluntary SEC deregistrations. *Journal of Accounting and Economics*, 45, 181-208.

Lewis, C., Kothari, S.P. (2022, Jun. 17). Comment on proposed SEC rule, "The enhancement and standardization of climate-related disclosures for investors." https://www.sec.gov/comments/s7-10-22/s71022-20132332-302895.pdf

Lewis, C., White, J. (2023). Deregulating innovation capital: The effects of the JOBS Act on biotech startups. *Review of Corporate Finance Studies*, 12, 240-290.

Li, T. (2018). Outsourcing corporate governance: Conflicts of interest within the proxy advisory industry. *Management Science*, 64, 2951-2971.

Matsusaka, J., Ozbas, O., Yi, I. (2021). Can shareholder proposals hurt shareholders? Evidence from securities and exchange commission no-action-letter decisions. *Journal of Law and Economics*, 64, 107-152.

Matsusaka, J., Shu, C. (2022). Does proxy advice allow funds to cast informed votes. USC Law Legal Studies Paper. https://ssrn.com/abstract=3866041

Malenko, A., Malenko, N. (2019). Proxy advisory firms: The economics of selling information to voters. *Journal of Finance*, 74, 2441-2490.

References (continued)

Malenko, N., Shen, Y. (2016). The role of proxy advisory firms: Evidence from a regression-discontinuity design. *Review of Financial Studies*, 29, 3394-3427.

Riedl, A., Smeets, P. (2017). Why do investors hold socially responsible mutual funds? *Journal of Finance*, 72, 2505-2550.

SEC (2020). Procedural requirements and resubmission thresholds under Exchange Act Rule 14a-8. https://www.sec.gov/rules/final/2020/34-89964.pdf

SEC (2022). Substantial implementation, duplication, and resubmission of shareholder proposals under Exchange Act Rule 14a-8. https://www.sec.gov/rules/proposed/2022/34-95267.pdf

Star, M. (1993). Powerhouse in New York. *Pensions & Investments*, 21, 2-41.

Uyeda, M. (2023, Jun. 21). Remarks at the Society for Corporate Governance 2023 National Conference. https://www.sec.gov/news/speech/uyeda-remarks-society-corporate-governance-conference-062123

Woidtke, T. (2002). Agents watching agents? Evidence from pension fund ownership and firm value. *Journal of Financial Economics*, 63, 99-131.

Data Appendix

Figure 1. Shareholder Proposals Voted Upon at S&P500 Issuers Over 2018-2022

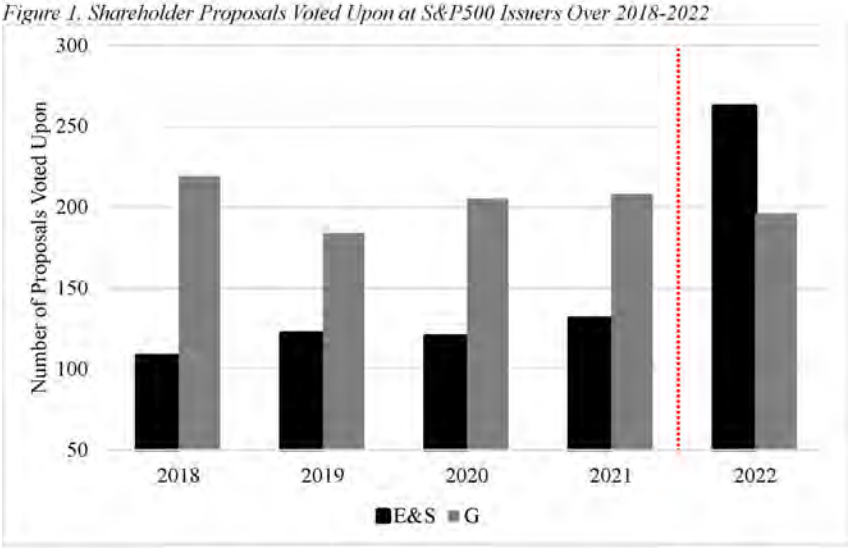
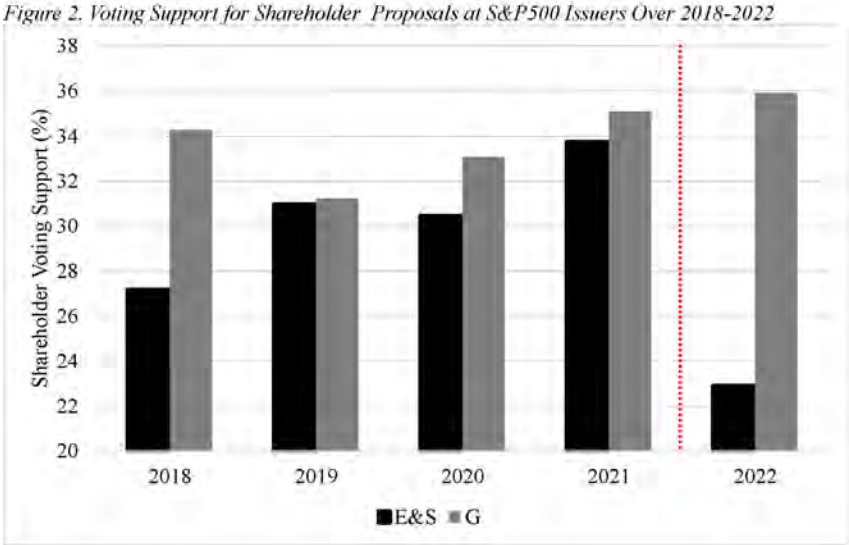


Figure 2. Voting Support for Shareholder Proposals at S&P500 Issuers Over 2018-2022



Data Appendix (continued)

Figure 3. Submitted Shareholder Proposals at S&P500 Issuers Over 2018-2022

Bipartisan Policy Center
Where democracy gets to work.

Question for the Record

"During the hearing Congressman Lucas (R-OK) asked you to describe the proxy process. Would you please briefly expound on the testimony you gave in response to his question."

Response by: Timothy M. Doyle, Senior Policy Advisor
Bipartisan Policy Center

Before the: U.S. House of Representatives
Committee on Financial Services
Subcommittee on Capital Markets

Hearing Title: "Reforming the Proxy Process to Safeguard Investor Interests"

Hearing Date: July 13, 2023

Proxy Process in Corporate Governance

In the context of corporate governance, the proxy process is a mechanism to allow beneficial owners (shareholders) the ability to vote either by mail or to designate a fiduciary to act as their agent to vote on their behalf at annual general meetings. This is a practical solution to avoid having shareholders attend multiple meetings scheduled at various companies across the country.

Since the growth of public markets from the 1900s, and in particular since the end of World War II, there has been constant tension between shareholder rights and corporate boards and executive management. This tension has been at the center of the proxy process and has correspondingly resulted in a long history of litigation. The tension has been amplified by the fact that, since the 1990s, the ownership of publicly traded companies has become much more concentrated through investments managed by institutional investors.

As mutual funds, exchange traded funds (ETFs), and pension funds continued to grow over the years, encompassing ever larger and more diverse sectors of publicly traded companies, there was a perceived need to vote on proposals in an increasing number of annual meetings. This need was bolstered by SEC regulatory action and the Department of Labor's issuance of the "Avon Letter" in the 1980s, which emphasized fiduciary duty and the importance of proxy voting. Ultimately, this need created the market for proxy advisors and their ability to review proxy materials at thousands of companies and provide analysis and recommendations. How they develop their recommendations and how those recommendations impact voting results is an issue of increasing concern.

Bipartisan Policy Center
Where democracy gets to work.

Furthermore, in conjunction with the proxy process, Rule 14a-8 of the Securities and Exchange Act of 1934 provides the framework for shareholders to request that their individual proposals be voted on at corresponding shareholder annual meetings. These proposals, if not otherwise excludable under 14a-8's provisions, would be included in the proxy materials provided to all shareholders before the next annual meeting.

As a result, the subject matter of suggested shareholder proposals and determining who ultimately decides how to vote on those proposals is increasingly debated. This issue is compounded by the fact that the beneficial owners of the shares have increasingly designated, by proxy, their voting rights to third parties, who in turn rely on proxy advisor recommendations for a variety of reasons. Further, under the current policy of the SEC, shareholder proposals dealing with broader societal issues, that might have otherwise been excluded under Rule 14a-8, are now being more readily included in proxy materials.

Conclusion

The changing process by which corporate policy is voted and acted upon makes the proxy process a vitally important part of corporate governance. The importance of the process has led to bipartisan calls for improving and reforming it for decades. Congress should continue to carefully analyze sustainable reforms to improve the proxy process.

7/20/2023
Rep. Dan Meuser

Questions for Jonathan Berry:
Most shareholder proposals today relate to environmental, social and political matters. At our hearing, some of the Democratic Members and one of the witnesses suggested that these issues are inherently tied to shareholder value and fall squarely within the fiduciary duty of institutional shareholders.

1. Have you seen evidence that the three primarily players in the proxy process (other than proponents) – the SEC, the proxy advisors and institutional shareholders – make decisions based on, or significantly influenced by, political perspectives?

    a. For example, do you see evidence that the SEC's no-action process, proxy advisor vote recommendations and institutional shareholder voting patterns are influenced by political perspectives? If so, please provide that evidence.

Answer of Jonathan Berry to Question 1: There is abundant direct and circumstantial evidence that key proxy-process actors operate with political bias. This skews the range of shareholder perspectives represented on the corporate ballot to overrepresent pro-ESG perspectives in the eyes of both shareholders and, importantly, managements and boards of directors. I discuss examples from the SEC's no-action process, proxy adviser vote recommendations, and asset manager and institutional investor voting patterns below.

SEC No-Action Process. The SEC has blocked many so-called "conservative" or "anti-ESG" shareholder proposals from consideration while rubber stamping its approval of pro-ESG proposals. For example, the Society for Corporate Governance observed in a recent comment to the Commission that, during the 2022 proxy season, the SEC granted no-action relief in 50% of the instances where relief was requested on "anti-ESG" proposals, compared with 38% across all proposals. The gap further widened when considering only social/political proposals, where the SEC granted relief at a 50% rate for proposals from "anti-ESG" proponents, as compared with 31% across all social/political proposals and 24% of environmental proposals considered by the SEC. As the Society commented, the disparity between these rates suggest "uneven grants of no-action relief . . . along ideological lines."[1]

A comprehensive study by Consumers' Research also confirms the SEC's viewpoint bias. During the 2018 through the 2022 proxy seasons, the SEC granted no-action relief under the ordinary business exclusion on 46% of all requests for liberal-aligned proposals in which it was raised, but 72% of all conservative-aligned proposals.[2]

---

[1] *See* Letter from C. Edward Allen, Vice President, Soc'y for Corp. Governance, to Vanessa A. Countryman, Secretary, SEC, Sept. 13, 2022, https://www.sec.gov/comments/s7-20-22/s72022-20142743-308679.pdf.

[2] *Consumers' Research SEC No-Action Audit 2018–2022* (May 4, 2023), https://consumersresearch.org/secnoactionaudit. These figures include proposals withdrawn by the shareholder proponent prior to the SEC issuing a no-action decision. If withdrawn proposals were subtracted, the disparity in no-action rates between liberal and conservative proposals would be even

The SEC has also granted companies relief to exclude conservative-aligned proposals even when they are almost identical to liberal-aligned proposals, such that there is no basis for any distinction between the proposals other than their respective political viewpoints. I respectfully refer you to the comparison table in my written testimony, which is reproduced below:

Conservative-Aligned Proposal SEC Determined Excludable	**Liberal-Aligned Proposal SEC Determined Non-Excludable**
Report on "the potential risks associated with omitting 'viewpoint' and 'ideology' from its written equal employment opportunity (EEO) policy."[3]	Report on "the potential risks associated with omitting 'sexual orientation' and 'gender identity' from its written equal employment opportunity (EEO) policy."[4]
Report describing "if and how the Company intends to reduce the risk associated with tracking, collecting, or shaping information regarding the processing of payments involving its cards and/or electronic payment system services for the sale and purchase of firearms."[5]	Report describing "if and how the company intends to reduce the risk associated with the processing of payments involving its cards and/or electronic payment system services for the sale and purchase of untraceable firearms, including 'Buy, Build, Shoot' firearm kits, components and/or accessories used to assemble privately made firearms known as 'Ghost Guns.'"[6]
Report on "prioritization of non-pecuniary factors when it comes to establishing, rejecting, or failing to continue network relationships on its [Company] platform." Supporting Statement notes the company "shutdown [a] conservative news network" "following a concerted campaign by liberal activists" who claimed the company was	Report on "human rights impacts of [Company] content management policies to address misinformation and disinformation across its platforms." Supporting Statement cites to policies designed to prevent "attempt[s] to interfere with elections or civic processes."[8]

higher given that more liberal proposals are withdrawn (ordinarily after company settlement) than conservative proposals.

[3] *The Kroger Co.*, 2023 WL 2060072 (SEC No-Action Letter, Apr. 12, 2023).

[4] *CorVel Corp.*, 2019 WL 1640021 (SEC No-Action Letter, June 5, 2019).

[5] *American Express Co.*, 2023 WL 2524429 (SEC No-Action Letter, Mar. 9, 2023).

[6] *Mastercard, Inc.*, 2022 WL 392206 (SEC No-Action Letter, Apr. 22, 2022).

[8] *Alphabet Inc. (W. Andrew Mims Trust)*, 2022 WL 392221 (SEC No-Action Letter, Apr. 12, 2022).

"consistently giving airtime to conspiracy and misinformation" such as "conservative conspiracy theories ... that the 2020 presidential election was stolen."[7]	
Report "on the risks created by Company business practices that prioritize non-pecuniary factors when it comes to establishing, rejecting, or failing to continue client relationships." Supporting Statement notes "[d]ebanking customers based on political, religious, or any other opinion or characteristic other than pecuniary advantage places the Company at great reputational, financial, and legislative and related risk" and "violates the Company's fiduciary duty to its shareholders."[9]	Request that the "Board of Directors take steps necessary to amend our certificate of incorporation ... to become a public benefit corporation." Supporting Statement notes that the proposal would "balance [the] interests of shareholders [and] stakeholders ... allowing the corporation to protect communities, even when it reduces financial return to shareholders in the long run."[10]
Requesting that companies publish their "diversity, equity or related employee-training materials" after they "adopt 'anti-racism' programs" that "distribut[e] pay and authority on the basis of race ... rather than by merit."[11]	Requesting that the company publish a "publicly disclosed" audit analyzing its "impacts on civil rights, equity, diversity and inclusion."[12]

Proxy adviser vote recommendations. The two proxy advisory firms that dominate the proxy advisor market, ISS and Glass Lewis, also exhibit clear patterns of bias in their proxy voting recommendations.

---

[7] *AT&T Inc.*, 2023 WL 108213 (SEC No-Action Letter, Mar. 15, 2023).
[9] *JPMorgan Chase & Co.* (SEC No-Action Letter, Mar. 21, 2023).
[10] *Alphabet Inc.*, 2021 WL 389302 (SEC No-Action Letter, Feb. 23, 2021).
[11] *See, e.g.*, *Verizon Communications Inc.*, 2022 WL 110304 (Mar. 17, 2022).
[12] *Amazon.com, Inc. (N.Y. State Common Ret. Fund)* (SEC No-Action Letter, Apr. 7, 2021), https://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2021/nyscrfamazon040721-14a8.pdf.

ISS. Based on data from ISS Voting Analytics, in calendar year 2022, ISS recommended a vote in favor of 6.3% of environmental, social or political proposals submitted by conservative-aligned proponents, while it recommended a vote in favor of 60.5% of environmental, social or political proposals submitted by other proponents (including liberal-aligned proponents). Similarly, during the 2023 proxy season (through July 25, 2023), ISS did not recommend a vote in favor of *any* environmental, social or political proposal submitted by a right-leaning proponent, while it recommended a vote in favor of 51.1% of environmental, social or political proposals submitted by other proponents.

Glass Lewis. Glass Lewis does not make its voting recommendations readily available, which makes it difficult to ascertain the firm's level of support for specific shareholder proposals. That said, Glass Lewis's Proxy Season Review 2022 indicates that Glass Lewis often supported environmental and social proposals in 2022, as well as all environmental and social proposals excluding right-leaning proposals.[13] Glass Lewis supported 39% of all shareholder proposals on social issues, though that level of support jumped to 47% when excluding proposals submitted by right-leaning proponents on social issues.

Statistically, it is improbable that such disparities in vote recommendations between proposals reflect actual differences in their benefits to companies and shareholders. These disparities are even more unjustified considering that liberal-aligned shareholder proponents often expressly disavow shareholder benefits in favor of collateral benefits, sometimes called "systemic" benefit. The only rational explanation for this discrepancy, in my view, is politics. If ISS or Glass Lewis disagrees with my conclusion, I invite them to share any economic analysis they conducted with respect to the environmental, social and political proposals they supported.

Asset Managers & Institutional Investors. We can observe voting trends among asset managers and institutional investors in general by looking at total vote outcomes for shareholder votes, since asset managers and institutional investors are generally the largest shareholders in public companies and therefore largely determine voting outcomes. According to data from ISS Voting Analytics, environmental, social and political topics submitted by conservative-aligned proponents received an average support of only 6.0% in 2022 and 2.5% in 2023 (through July 25, 2023). By contrast, environmental, social and political proposals submitted by other proponents received an average support of 29.3% in 2022 and 22.0% in 2023 (through July 25, 2023).

The results are similarly stark viewing how institutional investors voted on proposals by the 10 most prolific shareholder proponents which, according to a memorandum published by the law firm Sullivan & Cromwell LLP, accounted for over 60% of proposals submitted in 2022.[14] With respect to proposals submitted by the top 10 proponents, environmental, social and political proposals submitted by conservative-aligned proponents received average support of only 6.3% in 2022 and 2.5% in 2023 (through July 25, 2023). On the other hand, environmental, social and

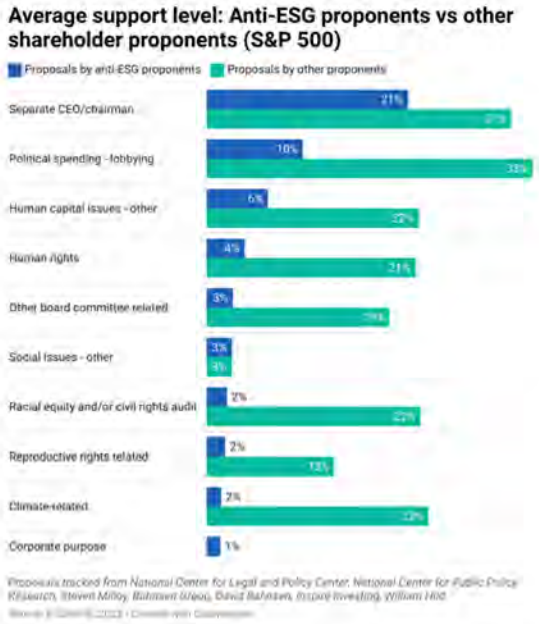
---

[13] See *Proxy Season Review 2022* at 59, Glass Lewis (2022), which I attach herein.
[14] *2022 Proxy Season Review: Part 1*, Sullivan & Cromwell LLP (Aug. 8, 2022), https://www.sullcrom.com/SullivanCromwell/_Assets/PDFs/Memos/sc-publication-2022-Proxy-Season-Part-1-Rule-14a-8.pdf

political proposals submitted by other proponents received average support of 34.2% in 2022 and 23.9% in 2023 (through July 25, 2023).

ISS Voting Analytics data also indicate that not a single environmental, social or political proposal submitted by a conservative-aligned proponent passed in either 2022 or 2023, while, when submitted by other proponents, 33 and 7 such proposals passed in 2022 and 2023, respectively.

A recent publication by The Conference Board covering the 2023 proxy season depicts the significant disparities in average levels of shareholder support by proposal:[15]



In these ways, the proxy process replicates in the private sector the same viewpoint discrimination against conservative viewpoints that the SEC does via government regulation.

---

[15] Paul Washington & Merel Spierings, 2023 Proxy Season: More Proposals, Lower Support, Harv. L. Sch. F. on Corp. Governance (June 1, 2023), https://corpgov.law.harvard.edu/2023/06/01/2023-proxy-season-more-proposals-lower-support/.

2. Given the proliferation of environmental, social and political proposals, is there a heightened risk associated with the duopoly of ISS and Glass Lewis having an outsized impact on voting results?

    a. In other words, is the duopoly in effect a "monopoly of thought" with respect to these social issues? For example, a 2023 report by the American Accountability Foundation titled "Proxy Wars: Glass Lewis" discusses the "liberal bias" of Glass Lewis that "goes a long way to help explain the success the far-left has had in forcing the implementation of ESG policies at major corporations in recent years."
    b. If you believe that there is a current or future risk of a "monopoly of thought" using the corporation to achieve ideological objectives, what do you think is the best legislative measure (or measures) to address this risk and depoliticize the corporation?

Answer of Jonathan Berry to Question 2: ISS and Glass Lewis have a tremendous amount of influence on proxy voting results. Once the SEC has approved pro-ESG shareholder proposals to be forced onto the corporate ballot, by their control of the proxy-voting market, these firms ensure that those proposals receive enough shareholder votes to win, or at least secure enough votes to increase shareholder proponents' leverage.

The trifecta of the SEC, the proxy advisors and the asset manager and institutional investors—each of which exhibit left-leaning biases in executing their respective roles in the proxy process—has resulted in a successful one-sided circumvention of the democratic process and a hijacking of the proxy machinery to advance the left's ideological goals, untethered from shareholder value. Ultimately, the broken proxy system negatively impacts the effectiveness of the capital markets and undermines the financial well-being of hard-working Americans regardless of their political affiliation.

I would like to highlight two legislative proposals that I believe would be especially helpful to solving the problems presented by political bias among proxy-process actors.

1. A prohibition on using Rule 14a-8 for environmental, social, and political proposals. In my view, Rule 14a-8 is not authorized by the Exchange Act, and, ideally, should be invalidated. However, short of a court or Congress invalidating the rule or the SEC rescinding it, Congress could limit some of the political viewpoint discrimination in the proxy process by taking politics out of the shareholder proposal process and prohibiting environmental, social, and political proposals.

As Congress considers legislation modifying Rule 14a-8, it should consider ways to ensure that such changes do not affirm Rule 14a-8 and inadvertently deny meaningful judicial review to the SEC's unlawful conduct in issuing and applying it to private market actors.

2. A requirement that proxy advisers, asset managers, and large institutional investors conduct and disclose an economic analysis when they reach conclusions contrary to the board's recommendations. Since proxy advisers, asset managers, and institutional investors

have demonstrated political bias when making vote recommendations and decisions, they should be required to publish their economic analysis for each proposal in which they recommended or voted against the recommendation of a primarily independent board of directors. There is a principled basis for this approach: Shareholders rely on an issuer's board (which has fiduciary duties to shareholders) to oversee all aspects of the corporation's management in shareholders' best interests; there is no reason for shareholders to second-guess the board's judgment with respect to environmental, social and political issues unless doing so is in best interests of shareholders. Requiring publication of proxy process actors' economic analyses would likely increase their accountability for their decisions.

United States

GLASS LEWIS

Proxy Season Review 2022

Key Trends, Season Highlights, Statistics & Notable Meetings

www.glasslewis.com

GLASS LEWIS

Table of Contents

About this Review 4
About Glass Lewis 5
Executive Summary 6
Key Trends 8
- Market/Regulatory 8
- Board and Governance Oversight 9
- Compensation 9
- ESG 10

Season Highlights 11
- U.S. Corporate Response to Invasion of Ukraine 11
  - Glass Lewis' Approach 11
  - Responses from Exposed Companies 11
  - Insufficient Responses from Exposed Companies 12
  - Downstream Effects of the Conflict 12
- Spotlight on ESG 13
  - Shareholder-Driven Environmental and Social Initiatives 13
  - Vote No Campaigns 13
  - Contested Elections 14
  - Director Accountability 14
  - Conclusion 15
- Multi-Class Share Structures: Putting an End to the Trend 16
  - A Necessary Shift in Policy 16
  - Alphabet and Meta: Lack of Board Accountability and a History of Corporate Governance Concerns 17
  - Prevalence of Multi-Class Share Structures 18
  - New Kids on the Block 18
  - Multi-Class Mega-Grants 18
  - Not All Multi-Class Companies Are Like the Others 19
  - Where Do We Go from Here? 19

Spotlight on Compensation 20
Top Dollar for Top Talent 20
JP Morgan Chase & Co 21
Rivian Automotive, Inc. and Lucid Group, Inc. 21
Proxy Statistics 23
Board Composition 23
Governance & Disclosure Trends 31
Election of Directors 37
Compensation Proposals 43
Shareholder Proposals 57
Notable Meetings 60
Director and Compensation Failures 60
Arrowhead Pharmaceuticals, Inc. (ARWR) March 17, 2022 60
G-III Apparel Group, Ltd. (GIII) June 9, 2022 60
Netflix, Inc. (NFLX) June 2, 2022 61
PacWest Bancorp (PACW) May 10, 2022 61
Tutor Perini Corporation (TPC) May 18, 2022 61
Election of Directors Protest Votes 62
Everbridge, Inc. (EVBG) May 19, 2022 62
Expedia Group, Inc. (EXPE) June 16, 2022 62
Natera, Inc. (NTRA) May 25, 2022 62
Silgan Holdings Inc. (SLGN) May 31, 2022 63
Twitter, Inc. (TWTR) May 25, 2022 63
Universal Health Services (UHS) May 18, 2022 63
Compensation Strikes 64
Norwegian Cruise Line Holdings Ltd. (NCLH) – June 16, 2022 64
Endo International plc (ENDP) – June 9, 2022 64
The Goodyear Tire & Rubber Company (GT) - April 11, 2022 64
CenterPoint Energy, Inc. (CNP) - April 22, 2022 64
Pebblebrook Hotel Trust (PEB) – May 16, 2022 65
Flowserve Corporation (FLS) – May 12, 2022 65

GLASS LEWIS

Appendix A 66
Appendix B 69
Appendix C 70
Appendix D 74
Connect with Glass Lewis 78

Editors & Contributors

Leon Bick
Brianna Castro
Joah Clements
Kayla Farriss
Erica Hylton
Courteney Keatinge
James McQuerrey
Doug Ryan
Krishna Shah
Aaron Wendt
Sarah Wenger
Dimitri Zagoroff

About this Review

Throughout the 2022 proxy season, Glass Lewis covered roughly 4,600 U.S. companies (consisting of shareholder meetings that took place during the six-month period from January 1 to June 30).

This review provides a comprehensive overview of the 2022 U.S. proxy season, with specific focus on data analysis of statistics, voting trends, season highlights and results. For further in-depth analysis of the 2022 proxy season, please see our season review on Shareholder Proposals for the U.S. market.

Clients can access our reviews via Viewpoint or Governance Hub, or by emailing their dedicated Client Services contact to request a copy. In addition, the data underlying this review is available in raw format – contact Glass Lewis for more information.

GLASS LEWIS

About Glass Lewis

Glass Lewis is the world's choice for governance solutions. We enable institutional investors and publicly listed companies to make sustainable decisions based on research and data. We cover 30,000+ meetings each year, across approximately 100 global markets. Our team has been providing in-depth analysis of companies since 2003, relying solely on publicly available information to inform its policies, research, and voting recommendations.

Our customers include the majority of the world's largest pension plans, mutual funds, and asset managers, collectively managing over $40 trillion in assets. We have teams located across the United States, Europe, and Asia-Pacific giving us global reach with a local perspective on the important governance issues.

Investors around the world depend on Glass Lewis' **Viewpoint** platform to manage their proxy voting, policy implementation, recordkeeping, and reporting. Our industry leading **Proxy Paper** product provides comprehensive environmental, social, and governance research and voting recommendations weeks ahead of voting deadlines. Public companies can also use our innovative **Report Feedback Statement** to deliver their opinion on our proxy research directly to the voting decision makers at every investor client in time for voting decisions to be made or changed.

The research team engages extensively with public companies, investors, regulators, and other industry stakeholders to gain relevant context into the realities surrounding companies, sectors, and the market in general. This enables us to provide the most comprehensive and pragmatic insights to our customers.

Join the Conversation

Glass Lewis is committed to ongoing engagement with all market participants.

info@glasslewis.com | www.glasslewis.com

GLASS LEWIS

Executive Summary

Dear clients, customers, and shareholders,

Proxy season 2022 was both predictable and unpredictable for the United States. Like in previous years that saw the beginnings of a global pandemic, "Great Resignation", the #MeToo movement, and rising climate concerns to name a few, at the start of this season AGM agendas were overshadowed by the broader sweep of events: in this case, the Russian invasion of Ukraine in February 2022. U.S. companies with Russian exposure were faced with the choice to leave entirely, provide a response and disclosure regarding continued sales and operations, or in some cases, not respond at all, which impacted proxy voting in 2022.

This review highlights key takeaways from the 2022 U.S. proxy season. Several of these trends predictably built on recent years' momentum in particular areas. For example, 2020 and early 2021 were marked by a significant rise in the creation of special purpose acquisition companies and initial public offerings. The subsequent increase in first year annual shareholder meetings continued this year and resulted in our coverage universe expanding to approximately 4,600 shareholder meetings in the United States. This represents an approximate 6% increase over the previous year. Nonetheless, our average lead time for U.S. reports remained the same as last year, at an industry leading 21 days ahead of meeting.

We observed an increasing number of companies respond to shareholder interest by disclosing board racial/ethnic diversity information. Approximately 95% of the S&P 500 disclosed this information at an aggregate or individual level this year, an increase from approximately 73% last year. Additionally, companies continue to improve their disclosures on environmental and social issues, as a staggering 88% of companies in the Russell 1000 specifically outlined their approach to board oversight of environmental and social issues. Shareholders also continued to demonstrate their expanding interest in environmental, social and governance (ESG) risks, through shareholder proposals, contested meetings and vote no campaigns. The total number of shareholder proposals increased by approximately 30% this year, with 100 more resolutions covering environmental and social issues than last year. We also observed an anticipated increase in the number of companies including environmental and social metrics in executive compensation incentive plans. All of these findings illustrate an increasingly shared view among investors and companies that effective oversight of material ESG risks is essential to ensuring the long-term sustainability of companies for all stakeholders.

There were also some surprises. For example, we observed a decrease in the number of directors leaving boards after failing to receive majority support from shareholders, after several years of increasing accountability. The impact from failed directors continuing to serve on boards, and boards rejecting such directors' resignations in increasing numbers, remains to be seen.

Engagement with public companies remains a focus for Glass Lewis. This proxy season, over 2,400 global companies used our Issuer Data Report to verify the accuracy of our data, and approximately 105 included their perspectives along with Glass Lewis research through our Report Feedback Statement service. Further, we continue to enhance our research, especially in the areas of environmental, social, and governance issues, through our Glass Lewis Controversy Alerts, which identify the most material meetings and votes; and through our ESG Profile and Data Feed, providing the timeliest information on public companies' performance and disclosure on key ESG topics collected at the time of their AGM.

GLASS LEWIS

Our focus at Glass Lewis will now shift to our post-season policy and product review and enhancements, along with client and issuer engagements. If you have any comments or feedback regarding this review, or if you are interested in accessing the underlying data that we have collected, please get in touch with your client service representative.

Warmest regards,

B. Castro

Brianna Castro

Senior Director, United States Research

GLASS LEWIS

Key Trends

Market/Regulatory

- Immediately following the February 2022 invasion of Ukraine, major global energy companies began to announce their exit from the Russian market. Shortly thereafter, we observed an exodus of exposed U.S.-based companies from Russia.
  - In total, 232 companies in our coverage disclosed exposure to Russia. A significant portion of these companies chose to exit Russia completely or provided a response and disclosure to investors we deemed suitable in light of their respective level of exposure. Four companies in our coverage provided responses regarding their exposure to Russia that we deemed insufficient and led us to recommend against directors.

- In March 2022, the Securities and Exchange Commission ("SEC") proposed rules to enhance and standardize climate-related disclosures for investors. The proposed rules would require companies to disclose governance of climate-related risks, material impacts on business and financial statements and future impacts on strategy and the impact of climate-related events, among other things.
  The proposed rules would also require disclosure of direct greenhouse gas (GHG) emissions (Scope 1) and indirect emissions (Scope 2) from purchased electricity or other forms of energy. Only certain companies would be required to disclose Scope 3 emissions.
  - On August 16, 2022, Glass Lewis submitted a comment letter to the SEC on Enhanced Disclosure of ESG issues and shortly thereafter published a corresponding blog post.

- The U.S. Holding Foreign Companies Accountable Act came into effect in 2021 and imposed a deadline for the PCAOB to inspect the auditors of U.S.-traded Chinese companies, as required by U.S. law. The law bans the trading of securities whose auditors can't be inspected by the PCAOB for three consecutive years, which China currently prohibits. In August, five Chinese state-owned companies said they would voluntarily delist from the New York Stock Exchange. The SEC has said that more than 270 U.S.-traded Chinese companies are at risk of delisting.
  - Many U.S.-traded Chinese companies are implementing governance reforms and pursuing dual-primary listings in Hong Kong in anticipation of a potential delisting from U.S. exchanges. We have already observed several Chinese companies in our U.S. coverage adopting "dual foreign names" and making other amendments to governing documents in preparation. Alibaba, among others, is one notable company with significant market value that has already received a first warning from the SEC.

GLASS LEWIS

Board and Governance Oversight

- The number of failed directors was largely static after a notable increase from 2020 to 2021. In total, 87 directors in our coverage failed to receive majority support this year, compared to 84 in 2021 and 67 in 2020. At Russell 3000 companies, the number of failed directors dropped slightly.
    - However, this season saw a sharp rise in the number of rejected director resignations and accompanying drop in the number of directors leaving boards after failing to receive majority support. Boards rejected 17 tendered resignations and only eight directors departed boards after failing to receive majority support, four less than last year.

- Board gender diversity concerns were a top driver of majority opposition to directors in 2022 and near the top of our most common withhold reasons. Glass Lewis is again raising the bar on gender diversity in 2023 as we transition to a gender diversity requirement of at least 30% for companies in the Russell 3000 Index. As of their 2022 annual meeting, more than 1,400 Russell 3000 boards in our coverage fall short of this mark. We will consider disclosure of diversity considerations and may refrain from recommending against directors of companies when boards have provided a sufficient rationale or plan to address the lack of diversity on the board, particularly when boards have disclosed a timeline to appoint additional gender diverse directors.
    - Board gender diversity continues to increase, albeit at a very slow pace. We observed a drop in the percentage of women among newly appointed directors this year. It is possible that some boards simply looking to comply with various state or exchange requirements may have paused searches for diverse directors once requirements were satisfied.

- Disclosure of board-level oversight of material environmental and social issues has become widespread among Russell 1000 companies. Further, shareholder focus on climate change has led to the expectation that companies disclose how boards are overseeing such risks that are material to their businesses.
    - Over 88% of Russell 1000 companies disclosed board-level oversight of environmental and social issues in their proxy statement. We recommended against directors at eight S&P 500 companies this year that did not disclose board-level oversight of environmental and social issues.

Compensation

- The percentage of failed U.S. say-on-pay votes increased to 3% in 2022, 20% above the number of failed proposals in 2021. Moreover, the number of companies that passed with low support (50% to 75%) increased by 38% from 2021.
    - Despite the aforementioned figures, the average shareholder support rate decreased by only 0.1% compared to 2021. This may be attributable to increasing numbers of say-on-pay proposals year-over-year with numerous IPOs and SPAC-mergers in 2020 and 2021. Newly traded companies holding their first advisory vote on executive compensation will often have the support of insiders in control of large holdings in the company. Their votes inflate support levels and dilute the impact of disinterested shareholder votes.

- Keeping in line with last year's results, the most common driver for Glass Lewis against recommendations was excessive granting/compensation in 2022. These practices were prominent for 12 out of the 19 S&P 500 companies that failed this year.
  - Low voting support was relatively predicable given the substantial increase in one-time awards and their values. Indeed, 2022 saw the highest dollar values for transaction, discretionary, promotion, sign-on and retention awards over the last three years.

- In 2022, E&S performance was included as part of the payout determination framework of short-term and/or long-term incentives for a majority of S&P 500 companies (61%) and Russell 1000 companies (52%), in all cases up from 2021.
  - While usage of E&S performance assessments continues to increase, the focus from shareholders is shifting toward disclosure of how E&S metrics are measured. This is particularly true for cases where performance has historically been determined on a largely subjective basis, particularly for human capital management and diversity.

ESG

- As a result of more permissive SEC rules, and the growing momentum around environmental and social issues, there was a roughly 30% increase in the number of shareholder proposals that went to a vote on a year-over-year basis, which included approximately 100 more environmental and/or social proposals than in the previous year.
  - Despite the significant rise in the number of proposals that went to a vote in 2022, shareholder support for a number of proposals across nearly all categories of shareholder proposals declined from previous years.

- There was a four-fold increase in the number of anti-ESG proposals that went a vote in 2022. These proposals, typically submitted by right-wing think tanks, are often aimed at reining in companies' environmental and social initiatives.
  - While 9 anti-ESG proposals went to a vote in 2021, 45 such proposals were featured on corporate ballots in 2022. These proposals received a notable increase in support, with average support rising from 3% to 9% in the last year, with four of these proposals receiving over 35% support.

- Although governance proposals are no longer the majority of proposals that go to a vote, they did represent a plurality of proposals in 2022, comprising 42% of all proposals that went to a vote in 2022, down from 64% the previous year.
  - There was a sharp rise in the number of special meeting proposals, and a commensurate decrease in the other types of governance proposals that went to a vote. During the 2022 proxy season, shareholders voted on 108 special meeting proposals, comprising just over 20% of all shareholder proposals that went to a vote in 2022.

Season Highlights

U.S. Corporate Response to Invasion of Ukraine

On February 24, 2022, Russian military forces entered Ukraine, thereby initiating what has since become a protracted invasion of the latter country. A preceding week of Russian aggression and escalation prompted a series of preliminary indictments, sanctions and travel restrictions from Russia's geopolitical peers, namely Australia, the European Union, Japan, the United Kingdom and the United States. Combined with widespread public scrutiny and subsequent economic sanctions by the U.S. Treasury, these measures have since sparked an exodus of exposed U.S.-based companies from Russia.

Glass Lewis' Approach

U.S.-traded public companies which have historically conducted business in Russia have had to decide whether to continue, suspend, or exit operations in Russia completely. Companies opting to continue business in the region could be exposed to operational, financial, or reputational risks. During the 2022 proxy season and moving forward, we are closely monitoring the actions and responses of companies that are materially exposed to the region. In the current political environment, we believe companies which continue to operate in Russia are likely to face increased scrutiny toward their approach, which may escalate to material reputational damage that could affect shareholder value.

When analyzing company responses throughout the 2022 proxy season, we considered, among other things, (i) whether the company provided any disclosure on its perceived risks of continuing operations in Russia, (ii) whether the company responded to any public shareholder concerns on its approach, (iii) the difficulty for the company to discontinue activities in Russia, and (iv) whether the company is providing essential products or services to Russian citizens.

Responses from Exposed Companies

Though we refrained from providing recommendations on companies which were the subject of sanctions, during the 2022 proxy season we identified approximately 232 U.S.-traded public companies in our research coverage with material exposure to Russia.

Among these exposed companies, 194 companies, or approximately 84 percent, provided shareholders with sufficient disclosure regarding their actions taken in response to Russia's invasion of Ukraine and the subsequent economic sanctions.

We considered a broad range of criteria when measuring companies' responsiveness. At minimum, we observed that responsive companies provided shareholders with disclosures regarding their outstanding investments and obligations in Russia, as well as the potential impact of the ongoing conflict thereon. These companies' disclosures tended to deemphasize the expected impact of Russian business on their overall business and profit expectations.

More thorough responses often included complete and indefinite withdrawals of operations, capital, and services from Russian territory. In more marginal cases, some companies even opted to fund Ukrainian aid and relief programs in addition to withdrawing services from Russia. Conversely, other companies such as Cloudflare, Inc. remained responsive to sanctions by limiting payments received from sanctioned Russian accounts while still electing to maintain its commercial activity within the region. Though the company has argued for the benefit of preserving its internet services for Russian citizens during this time, we believe shareholders ought to be mindful of the reputational risks associated with this limited response.

During the proxy season window, PayPal Holdings, Inc. served as a leading example of a robust corporate response to the invasion. On March 5, 2022, the company announced that it would be suspending its services in Russia and began waiving transfer fees for its Ukrainian users starting on March 17, 2022. Since then, PayPal and its various charity partners have together contributed over $420 million to support humanitarian relief in Ukraine.

Insufficient Responses from Exposed Companies

The remaining 16 percent of exposed companies either did not respond to the Russian invasion of Ukraine at all or, in several marginal cases, maintained their business presence in Russia without providing sufficient explanation. Chubb Limited is a prominent example of a company within the latter group. As of the publication of our proxy paper covering their 2022 annual meeting, the company had not addressed the continued business presence of two of its subsidiaries, Chubb Insurance Company LLC and Chubb Life Insurance Company LLC, in Russia. Furthermore, the company maintains a 23 percent ownership in the Russian Reinsurance Company.

In certain cases where we concluded that shareholders weren't provided with sufficient disclosure on the risk assessment made for continuing a company's Russian business operations, we recommended that shareholders cast votes against the board or governance committee members. While an overwhelming majority of exposed companies in our research coverage provided shareholders with a sufficient response regarding their business exposure, four companies failed to provide shareholders with a response we considered sufficient. Specifically, we recommended shareholders vote against board or governance committee members at the 2022 annual meetings of International Paper Company, IPG Photonics Corporation, Match Group, Inc., and Titan International, Inc.

Downstream Effects of the Conflict

Very few U.S. companies maintain outsized levels of investment in Russia as compared to their other domestic or international investments. As such, there does not appear to have been a widespread, long-term impact on market value or business operations among these U.S.-traded, exposed companies, regardless of their responsiveness. However, as the Russian economy continues to bear the weight of sanctions, we anticipate that companies which further opt to cultivate their Russian business ties may suffer some reputational harm that could contribute to losses in shareholder value.

The scope and nature of the sanctions imposed on Russian companies and individuals are still changing and evolving, as are societal expectations for non-Russian businesses to sever ties with Russia. Glass Lewis continues to monitor these sanctions, as well as the broader governance implications of the conflict. Further, we believe that shareholders can reasonably expect periodic updates from impacted companies as the war progresses. The

extent to which shareholders will use the proxy process to hold boards accountable for their response to these far-reaching issues, and global events more generally, remains unknown; however the institutional response to date serves to illustrate that the proxy process remains a viable tool for investors when global events necessitate corporate responsiveness.

Spotlight on ESG

The 2022 proxy season continued to see a rise in disclosure concerning environmental, social and governance issues in proxy statements in correlation to shareholders' ongoing focus on these topics. While governance and compensation issues have historically been primary areas of focus for investors, there has been a notable shift to include environmental and social considerations, including how these matters are overseen at the board level.

Shareholder-Driven Environmental and Social Initiatives

Unsurprisingly, an increased interest in these issues resulted in increased shareholder environmental and social initiatives. Following the upward trend, the 2022 U.S. proxy season contained the largest number of shareholder proposals seen in recent years, with a 27% increase from last year. This is primarily due to the SEC's changing approach to no-action requests, making it more difficult for companies to exclude certain shareholder proposals.

Vote No Campaigns

However, the impact goes beyond shareholder proposals. At the same time, many investors have incorporated more environmental and social considerations in their voting policies and are actively looking at board oversight over these matters. Although voting against board members is a common way to express shareholder dissatisfaction regarding traditional corporate governance and compensation concerns, targeting directors for ESG matters is still a relatively new concept, but one that is growing in popularity.

Part of the growth in voting against directors on environmental and social grounds has been fueled by a growing number of "vote no" campaigns, in which shareholders or activist groups encourage investors to vote against directors at companies where they have identified environmental and social risks or underperformance. For example, Majority Action, a climate-focused NGO issued the largest number of "vote no" campaigns throughout the 2022 season, targeting at least 20 companies and urging shareholders to vote against approximately 40 directors they believe demonstrated insufficient oversight of climate risks. Of the targeted companies, the majority operate in the energy sector, including ExxonMobil Corp., Chevron Corp. and Kinder Morgan, Inc.; however, this year Majority Action widened its scope to include additional major financial institutions, such as JPMorgan Chase &Co., The Goldman Sachs Group, Inc., and Wells Fargo & Company. On average, directors targeted by Majority Action received 91% support from shareholders.

Although many vote-no campaigns have traditionally been focused on environmental issues, there was a growing focus on social issues over the last year. For example, in April 2022, the Comptroller of the City of New York launched a campaign urging shareholders to vote against two directors at Amazon.com, Inc., both longstanding members of the leadership development and compensation committee, for what the Comptroller believed to be a failure to exercise adequate oversight of Amazon's human capital management practices.

Further, in May 2022, the SOC Investment Group urged shareholders to vote against the election of six directors at Activision Blizzard, Inc., including CEO Bobby Kotick, for what it believed to be an inadequate response to the company's sexual harassment crisis and a failure to appropriately address Activision's culture. The targeted directors at Amazon.com, Inc. received 93% and 78% support from shareholders, while the six targeted directors at Activision received support ranging from 72%-89%.

Overall, it appears that shareholders are increasingly willing to express their concerns about companies' E/S risks and oversight through director elections, as several of these directors targeted in social risk driven vote no campaigns were opposed by over 20% of shareholders, and all but one were opposed by at least 10% of shareholders voting at the annual meetings.

Contested Elections

Another form of shareholder resistance is demonstrated through contested elections. Investors are becoming more willing to use these contests as an opportunity to dispute key points of contention, including insufficient action on environmental and social issues, following the example of Engine No. 1 set at ExxonMobil's 2021 contested director elections. Although none were as successful as the campaign launched at Exxon, there were a number of attempts at changing the board composition of companies where activists identified significant environmental and social issues.

Arguably, the most notable of these was at Guess?, where the dissident cited ongoing claims of sexual misconduct and related concerns by the firm's chief creative officer. While this did receive notable support, it was not enough to overcome the strong inside ownership of the founders, who own an approximate aggregate 41.5% of the company's outstanding common stock (and one of whom was the subject of allegations in this campaign).

However, in stark contrast to the contests at Guess? and Exxon, two campaigns focused on issues of animal welfare did not garner strong shareholder support. In advance of their 2022 meetings, affiliates of Carl Icahn announced that they would be contesting the elections of members of the board of McDonald's Corporation and The Kroger Co., largely based on the use of gestation crates within their pork supply chains. At McDonald's, the earlier of these two meetings, the dissident directors received less than 2% shareholder support, which was likely the reason why the campaign at Kroger was withdrawn prior to its annual meeting.

Director Accountability

There is a growing expectation among investors that boards should maintain oversight of a company's material environmental and social risks, and companies are increasingly meeting this. In 2022, 88.6% of companies included in the Russell 1000 index disclosed board oversight of environmental and social issues, a staggering 31% increase from last year and 37% increase from 2020. While we have tracked companies' disclosure of environmental and social oversight for several years, this year, Glass Lewis began recommending voting against directors at S&P 500 companies who provided no disclosure of this oversight function. Of the companies in the S&P 500 index, 98.4% provided some level of disclosure of environmental and social oversight. Just eight companies (1.6%) did not provide explicit disclosure.

In addition, for a number of years, Glass Lewis has recommended voting against directors at U.S. companies in instances where we believed that companies' management of environmental or social risks has threatened shareholder value. For the second year in a row, Glass Lewis has increased the number of such recommendations. For example, Glass Lewis recommended against directors serving on the board of Berkshire Hathaway, Inc. on account of a significant and notable lack of disclosure on climate-related risks. We also issued recommendations at companies including Amazon.com Inc., Johnson & Johnson and The Boeing Company, in response to concerns regarding human capital management, ongoing litigation and reputational risks, and product safety, respectively.

In addition to managing and overseeing environmental and social risks, we believe directors have a responsibility to engage with shareholders on these matters and respond appropriately to related concerns. This response is particularly important when companies receive strong support for shareholder proposals. In 2021, there was a notable increase in the number of majority-supported shareholder resolutions on environmental and social issues. However, companies' response to this shareholder sentiment varied significantly. Of approximately 25 companies that had a majority-supported shareholder proposal, only two failed to respond adequately.

When companies fail to engage with shareholders in the presence of high opposition, or sufficiently respond to a majority-supported shareholder proposal, we will generally recommend voting against directors. In our view, we saw an insufficient response to majority-supported proposals at Bloomin' Brands, Inc. and Wendy's Corporation, which resulted in negative recommendations against the chair of their nominating and corporate governance committees. We also encouraged shareholders to withhold from the chair of the board at Sturm Ruger & Company, Inc. in response to concerns regarding its engagement with the proponent of a shareholder resolution as well as its general responsiveness to shareholder concerns. In our view, companies should be not only be engaging in an ongoing dialogue with shareholders, but also providing disclosure to that effect, as it helps to promote transparency, robust governance structures and companies' responsiveness to, and engagement with, their shareholders.

A notable example of responding to shareholder feedback occurred at Netflix, Inc., which has, for multiple years, failed to implement majority-supported shareholder proposals dealing with matters including declassifying the board, shareholders' ability to call special meetings, and removing supermajority vote requirements. However, in 2022, Netflix, Inc. introduced several governance-related reforms aimed at addressing this longstanding shareholder sentiment.

Conclusion

It is our view that every company faces material ESG-related risks, and that a failure to mitigate these risks, or fully allow shareholders to understand these risks as they are making their investment decisions, has the potential to result in loss of shareholder value. Glass Lewis therefore believes that effective and robust oversight of ESG risks is critical to ensuring the long-term viability of companies. It is clear, as demonstrated through votes on shareholder proposals and on directors, that many investors share this view.

As the market's understanding of material ESG-related continues to deepen, there is an increased expectation that companies are both providing disclosure concerning their ESG considerations and that they are providing

adequate oversight of the issues most relevant to their operations. Many investors also acknowledge that companies that have not provided for this disclosure or oversight are increasingly viewed as laggards in this regard. Therefore, it is critical that companies monitor not just their own ESG-related risks, but also the evolving expectations of investors and the market.

Multi-Class Share Structures: Putting an End to the Trend

For most investors, "one share, one vote" structures remain the gold standard in corporate governance. However, of late, some have favored purportedly visionary founders and stocks that "pop" on IPO day in lieu of fundamental shareholder rights.

Since Google's IPO in 2004 (now known as Alphabet Inc.) and Facebook's IPO in 2012 (now known as Meta), companies have increasingly been going public with multi-class share structures. Multi-class share structures allow founders and other significant pre-IPO shareholders to maintain control over a company through super-voting shares while reaping the rewards of reducing their economic stake. In many cases, multi-class share structures are closely linked to reduced shareholder rights and lesser board and management accountability. Concentrated voting rights at these companies causes minority shareholders to have an unequal voice in corporate oversight and management. Further, this lack of accountability can foster an environment that leads to issues with workplace culture and corporate scandals.

Companies looking to follow in the footsteps of Google and Facebook have modeled their capital and governance structures after the two tech behemoths. As more and more companies enter public markets with multi-class share structures and poor governance, our concerns reached a tipping point in the past year. Following a record number of IPOs in 2021, we have observed a considerable number of companies going public with these insular capital structures, only to have governance concerns and controversies crop up and harm shareholder value.

A Necessary Shift in Policy

Previously, Glass Lewis only recommended withholding votes from directors due to multi-class share structures at the first annual meeting after a company's IPO. However, given the significant increase in companies with multi-class share structures, Glass Lewis has adopted a policy targeting companies that have multi-class share structures with unequal voting rights and lack proper safeguards for shareholders.

Beginning with the 2022 proxy season, we typically recommend voting against the governance committee chair at companies that have a multi-class share structure and unequal voting rights without a reasonable sunset provision. We consider time-based sunset provisions (generally seven years or less) whereby super-voting share classes will convert into common stock automatically and carry one-vote per share thereafter to be reasonable. Glass Lewis strongly prefers "one share, one vote" structures, which ensure that shareholders' economic stake matches their voting power and serves as a safeguard so that minority shareholders can weigh in on issues set forth by the board.

Alphabet and Meta: Lack of Board Accountability and a History of Corporate Governance Concerns

Meta and Alphabet are two examples of the voter disenfranchisement associated with multi-class share structures, as both companies have super-voting share classes controlled by their founders.

Since 2018, Meta has struggled to repair its reputation after a whistleblower revealed that Cambridge Analytica shared Meta users' data without their knowledge. The data breach prompted government inquiries in the United States and the European Union as well as investigations by the SEC, FBI, and FTC. Yet the Cambridge Analytica scandal was neither the first time Meta faced such issues nor the first time it faced regulatory scrutiny; clearly, ongoing concerns are falling on deaf ears.

Meta's allegedly unethical behavior and disregard for shareholder concerns are evident in the numerous shareholder proposals that receive high support from unaffiliated shareholders but ultimately do not pass due to the multi-class voting structure. Specifically, at the 2022 annual meeting, a shareholder proposal calling for the elimination of the multi-class structure would have received support of approximately 74.7% from unaffiliated shareholders if the Class B shares carried only one vote per share, yet the proposal failed to pass given the super-voting Class B shares.

The multi-class share structure also impacts Meta's board composition. Peggy Alford and Marc Andreessen serve as "independent directors" despite their prior employment with the Chan Zuckerberg Initiative and business dealings with Meta, respectively. This affiliation raises eyebrows, particularly given that Alford was opposed by nearly 20% of votes cast by unaffiliated shareholders at the 2022 annual meeting, reflecting concerns about her performance on the audit committee and her role in risk management oversight. The share structure insulates the board and management from investor feedback and underscores our concern regarding the board's inadequate protection of shareholder rights.

Despite shareholders' continual cry for change, Meta has not, to our knowledge, directly addressed the votes cast by unaffiliated shareholders in any of its communications. Instead, then-Facebook chose to distance itself from past controversies and scandals by changing its corporate name to Meta Platforms in late 2021.

Alphabet faces many similar challenges. For example, at its 2022 annual meeting, several proposals received majority support from unaffiliated voting shareholders when evaluating the vote results on a "one share, one vote" basis. Approximately 76.8% of votes cast by unaffiliated shareholders were in favor of a proposal to eliminate Alphabet's multi-class share structure, yet once again the proposal failed due to the multi-class share structure.

Additionally, at Alphabet's 2020 annual meeting, the advisory vote on executive compensation would have received the support of approximately 43% of votes cast by unaffiliated shareholders. However, with the super-voting share classes, it passed with a 75% majority vote. Advisory votes on executive compensation at Alphabet are held every three years; therefore, the issue was not on the 2022 ballot. The lack of an annual advisory vote on executive compensation further disenfranchises shareholders and weakens Alphabet's overall governance practices.

All these votes fail to incorporate shareholder input from Alphabet's largest class of common shares (non-voting Class C) and indicate extraordinary shareholder dissatisfaction with aspects of Alphabet's general corporate governance, compensation programs and practices, and voting structure. Like Meta, Alphabet has not, to our knowledge, directly addressed the votes cast by unaffiliated shareholders in any of its communications.

Prevalence of Multi-Class Share Structures

We reviewed more than 350 companies with multi-class share structures in our coverage during the 2022 proxy season. Among these companies, 22 were in the S&P 500 and 82 were in the Russell 1000. Time-based sunset provisions proved to be uncommon, as only 61 multi-class companies in our coverage have time-based sunset provisions. Even when time-based sunset provisions are present, the duration is often extensive, with just 38 limited to seven years or less. The trend does not appear to be changing: of the 65 companies in our coverage that went public with multi-class share structures in 2021, 43 companies have no sunset provision and only nine have sunset provisions of seven years or less.

During the 2022 proxy season, we recommended that shareholders vote against directors at 202 companies (19 in the S&P 500 and 58 in the Russell 1000) that have multi-class share structures with unequal voting rights and lacked the proper safeguards. In certain cases, we made exceptions to our policy for companies with alternative multi-class voting structures or other notable safeguards.

New Kids on the Block

AirBnB and Robinhood are examples of recently public companies with multi-class share structures leading to governance and oversight concerns.

Airbnb has one of the most outsized share structures of companies we reviewed; each Class B share carries 20 votes. Governance concerns at AirBnB include insufficient board and committee independence, which could be contributing to a lack of proper oversight at the company. AirBnB has been the target of public criticism over privacy concerns, cover ups of scandals on their rental properties, and the company's effect on housing and rent prices.

Since inception, Robinhood's slogan has been "democratize finance for all," with its co-founders claiming they sought to make equity markets more accessible to everyday investors. Yet the company has failed to live up to those ideals: founders own only 15% of the company's shares, but control 63% of the voting power. This inequality stands in stark contrast to the company's stated aim of democratizing finance. The unusual amount of power granted to the co-founders is especially troubling given recent regulatory interventions, including fallout from the GameStop "meme stock" trading frenzy and Robinhood's widely criticized subsequent decision to restrict trading in some stocks.

Multi-Class Mega-Grants

The Trade Desk and Rivian Automotive, which went public in 2017 and 2021, are two companies with multi-class share structures where lack of proper oversight could be contributing to concerns over their compensation practices, including mega-grants made to their founders and CEOs.

The multi-class share structure at The Trade Desk has enabled poor compensation practices and mega-grants made to its CEO. Indeed, one pension fund sued The Trade Desk's board and billionaire CEO, accusing him of abusing power to force through one of the largest compensation grants in history. The complaint also alleges a breach of fiduciary duties to shareholders in connection with amendments to the company's certificate of incorporation and matters pertaining to the voting structure.

In May 2022, SOC Investment Group filed an exempt solicitation urging shareholders to vote against Rivian's "say on pay" proposal and questioned the size of the CEO's 2021 performance award given that the CEO already owned significant pre-IPO equity that will appreciate if the company performs well.

Not All Multi-Class Companies Are Like the Others

As with all our policy recommendations, we consider circumstances on a case-by-case basis. Several factors impact our analysis that may lead us to make exceptions to our policy, including whether additional share classes are tenure-based, how widely held additional share classes are, and whether companies include caps on voting power, among other things. Aflac and United Parcel Service are two companies with multi-class share structures that included certain mitigating factors which alleviated our concerns and led us to make exceptions.

When additional share classes are not designed to preserve voting control for certain shareholders indefinitely or there is no concentration of voting power in the hands of one or a few holders, our concerns are lessened as compared to other multi-class share structures. When companies have unique voting structures or certain safeguards in place, we look for clear disclosure in proxy statements that sufficiently explain the voting mechanisms to shareholders.

Where Do We Go from Here?

Multi-class share structures without reasonable sunset provisions are becoming increasingly common. With no regulations or restrictions, U.S. markets and exchanges are largely accepting multi-class share structures. Companies and founders have little reason to deviate from current trends if investors continue to forgo their voting power in favor of investing in the next so-called unicorn.

In October 2021, the Council of Institutional Investors submitted draft federal legislation targeted at companies with multi-class share structures. The draft legislation would prohibit the listing of companies in the United States with unequal voting rights and no time-based sunset provision of seven years of less, unless shareholders of all classes of stock approved the unequal share structure. The bill is being considered by a panel of the U.S. House of Representatives. Other shareholder advocates wrote to congress in support of the bill, including the New York State Comptroller and the Ohio Public Employees Retirement System.

As such, Glass Lewis is targeting directors at companies with multi-class share structures that have unequal voting rights. Moreover, we emphasize the need for proper safeguards to prevent unchecked voting power from leading to a deterioration in shareholder rights, or even worse, the next corporate controversy that destroys shareholder value.

Spotlight on Compensation

Top Dollar for Top Talent

Pay decisions influenced by the impact of the pandemic shifted in 2022. In-flight adjustments to existing incentives, the heightened reliance on committee discretion on payouts, and switches to less performance-based vesting structures were the hallmarks of the 2021 proxy season as companies responded to perceived retention risks due to the economic shockwaves of 2020. By contrast, the 2022 proxy season marked a new wave for compensation trends — this time to respond to the side effects of 2020's shutdowns and slowdowns.

Labor markets have yet to fully recover from systemic worker shortages. Snarled supply chains delayed the delivery and raised the cost of materials and finished products. Geopolitical tension deepened the cracks in the global economy with rising energy prices. It seemed too much for America's highest paid executive talent to bear.

While stubborn operational challenges remained unresolved, the competition for executive talent who were apparently in search of even greener pastures turned fierce. Executive retention became increasingly untenable, according to many corporate disclosures. To encourage executive engagement and commitment to solving current corporate problems, fretting companies opened their wallets wider.

Special retention awards were very common in 2022. Not only did the number of retention one-time awards increase 38% from 2021 and 2020 figures, but the average value of such awards also spiked by approximately 112% from 2021 and 183% from 2020. Companies that granted these awards cited the need to retain executives through macroeconomic uncertainty, a highly competitive market for talent, and even the "Great Resignation."

One might worry, meanwhile, that based on their frequency in 2022, mega-grant versions of retention awards appeared close to a tipping point in U.S. executive pay practices. Such awards are characterized by massive valuations, typically but not always subject to generally longer time horizons. In some cases, the first vesting tranche of a mega-grant qualified as a mega-grant on its own. One of the largest awards in 2022 was over $800 million granted to Trade Desk CEO, Jeff Green. The impetus for many mega-grants were concerns about retention and the desire to incentivize sky-high performance with sky-high pay. The most recent proxy season might not be the end of it. The inclusion of these mega-granting companies in peer comparisons and benchmarking will only encourage other companies to follow suit. However, if 2022 disclosure of benchmarking practices is any indicator, the negative shareholder sentiment for problematic pay decisions of peers, evidenced by Intel Corp's back-to-back say-on-pay fails in 2021 and 2022, will largely be left out of the central discussion.

Year-over-year increases in average and median total direct CEO pay between 2022 and 2021 for S&P 500 companies were approximately 17% and 21%, respectively, compared to a change of 13% and 0%, respectively, between 2021 and 2020. While the market continues to coalesce around a "new normal", one fact remains true. Recession or expansion, shutdown or ramp-up, U.S. executive compensation rises. Perhaps it is only the rationale that changes. It is no coincidence that excessive granting and compensation continued to be the most common driver for Glass Lewis' against recommendations.

JP Morgan Chase & Co

Background

Has the Great Resignation reached the C-Suite? If you were basing your answer on the actions of compensation committees, you may think the answer is a resounding yes. Boards appear to be trying to mitigate any potential turnover, granting an increasing number of awards with rising values, often on the basis of retention concerns. In 2021 this included one of America's Too Big to Fail Banks, JPMorgan Chase & Co., which granted substantial one-off awards to both its CEO, James Dimon, and COO, Daniel Pinto.

Mr. Dimon's retention award and Mr. Pinto's promotion award had disclosed values of approximately $52.6 million and $27.9 million, respectively. Both awards, at least in part, reflected the committee's desire for the executives to continue in their roles for a significant number of years. The company recently parted ways with Mr. Pinto's co-COO.

These awards were subject to five-year cliff vesting, with net shares subject to a holding period until the tenth anniversary of the grant date. Further, up to 50% of the award is contingent on what the company refers to as protection-based vesting, which provides for the potential cancellation of that portion of the award if certain performance conditions related to individual performance or company performance were not met. We noted, however, that these were largely extensions of the company's clawback policy and fell short of being a suitable replacement for regular performance-based vesting conditions.

What is an Executive Worth?

While there may be reason for concern related to NEO turnover in recent years, actions that drive a potential wedge between pay and performance should still draw heightened scrutiny. Given the prior concerns surrounding the alignment of pay-with-performance at JPMorgan in recent years, the decision to use largely performance-insensitive awards with excessive values raised questions regarding the alignment of pay with performance in the near future.

JPMorgan is far from alone in granting sizeable one-off awards for the disclosed purpose of incentivizing retention. However, given their quantum and structure, the awards granted to Messrs. Dimon and Pinto were particularly problematic for shareholders. Despite belonging to an industry that is known for its generous compensation practices, the company earned only 31% support for its say-on-pay proposal, compared to 90% in 2021. With this, JPMorgan joined the ranks of 18 other S&P 500 companies that failed their say-on-pay in connection with excessive granting practices.

When considering the question of what an executive is worth during times of uncertainty, companies and shareholders alike may view the response to JPMorgan's answer as a cautionary tale.

Rivian Automotive, Inc. and Lucid Group, Inc.

Background

When it comes to compensation practices, is there a contagion effect? Based on the growing number of mega-grants, it could be reasonable to think so. Two major electric vehicle companies that went public in 2021 are prime examples. Lucid Group, Inc. became a public company through a SPAC merger in July, and Rivian

Automotive, Inc. conducted a more traditional IPO in November. They wasted no time drawing attention for mega-grants made to their respective CEOs prior to going public.

Robert J. Scaringe, Rivian's CEO, received a mix of time-based and performance-based stock options with a reported value of $241 million at the time of grant in January 2021. Lucid granted RSUs and PSUs with a reported value of approximately $556 million to their CEO, Peter Rawlinson. The awards they received exemplified the recent trend of mega-grants.

The Rising Cost of "Creating" Shareholder Value

For Rivian, the concerns centered on the sheer quantum of pay. While a majority of the options were subject to substantial stock price targets, the staggering value of these awards, as well as the 2.9% dilutive impact of this single grant, were eye-watering.

Size was an issue with Lucid's mega-grant as well, but in that case concerns were also raised about the performance-based vesting structure. Under the terms, Mr. Rawlinson could potentially receive a windfall based on a particularly strong six months, without requiring sustained long-term performance. Indeed, subsequent events reinforced this concern. In March 2022, less than a year after the company's July 2021 debut as a publicly traded company, the board deemed four of the five market capitalization hurdles achieved. A quick glance at Lucid's stock chart shows that this performance was not sustained for long, as the market frenzy around electric vehicles settled down.

The price tag of the awards to both Messrs. Scaringe and Rawlinson warranted close examination. In fact, Rivian became the focus of a Vote No campaign for its first advisory vote on executive compensation. Meanwhile, the structure of Mr. Rawlinson's award and the quick earn-out events may call into question whether these types of costly awards create long-term shareholder value, a common rationale for mega-grants.

Aberration or Acceptance?

Despite the problems with quantum and structure, shareholders supported the say-on-pay proposals for each company, at levels exceeding 90%. This notably contrasts with the significant levels of opposition seen for well-established public companies that have made mega-grants in recent years, including the likes of Intel, Paycom and ServiceNow.

Both companies' vote results may indicate that shareholders are willing to grant a wider degree of latitude to newly public companies, or perhaps only for ones with extraordinary growth potential as is the case of the electric vehicle space. It remains to be seen whether shareholders will continue to support mega-grants tied to the potential of newly traded companies, but the results at Rivian and Lucid seem to indicate as much.

GLASS LEWIS

Proxy Statistics

Board Composition

Key Findings

- Over the past three years the number of companies with no women on their board has dropped by almost half. Most boards in our coverage have between 11-30% women. Committee chair positions held by women have increased considerably over the past three years with women chairing 32% of nominating and governance committees.
- S&P 500 boards in our coverage averaged 23.4% racial/ethnic diversity while Russell 1000 boards averaged 22.1%. Among S&P 500 boards that disclose information about diversity, those with no racially/ethnically diverse directors are outliers, comprising just 0.25% of total.
- Public company directorship numbers have stabilized and the number of directors serving on one board has hovered around 68.0% for the previous three years. Approximately 99.4% of directors in our coverage serve on four boards or less. Overboarded directors remain extreme outliers.

2022 U.S. Board Statistics at a Glance

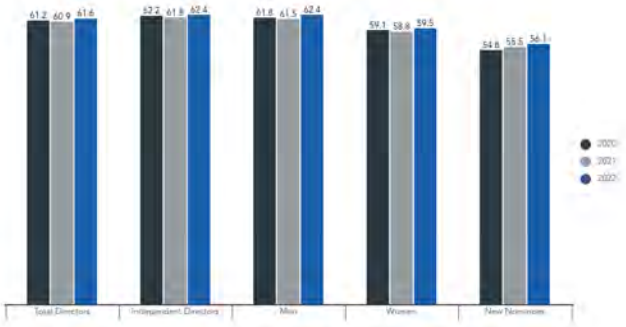
Total Companies in Glass Lewis Coverage	Approx. 4,600
Total Directors	36,661
Average Board Size	8.7
Average Independence	76.3%
Average Percentage of Women on Board	25.9%
Independent Chair (chair only; excludes vice-chair or lead directors)	42.8%

GLASS LEWIS

Russell 3000 Index	Men	Women
First Year Appointments	57.9%	42.1%
Gender (Im)Balance	71.9%	28.1%
Percent of Independent Directors	67.0%	33.0%
Directors		
Average Age	62.4	59.5
Average Tenure	8.9	5.3
Average Directorships	1.4	1.6
Board Leadership		
Chair	92.3%	7.7%
CEO	93.6%	6.4%
Lead Director	87.0%	13.0%
Audit Committee Chair	73.0%	27.0%
Compensation Committee Chair	73.4%	26.6%
Nom/Gov Committee Chair	77.9%	32.1%

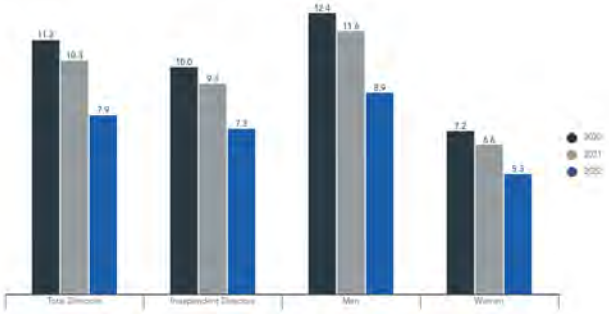
GLASS LEWIS

Russell 3000 - Average Director Age



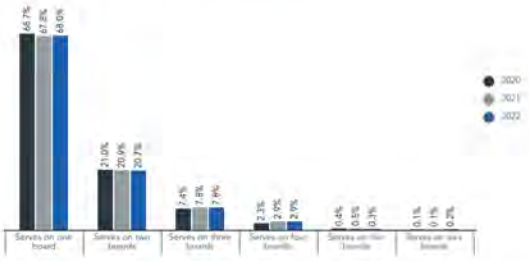
Average director tenure continues its downward trend as board refreshment among Russell 3000 companies has brought average director tenure down by more than three years since 2020.

Russell 3000 - Average Director Tenure



GLASS LEWIS

Russell 3000 Directors - Number of Public Company Directorships



Out of the more than 18,000 directors serving on Russell 3000 boards in our coverage, only 30 of these directors serve on six or more boards. Approximately 99.4% of these directors serve on four boards or less. Voting trends among shareholders have driven average directorship numbers down in recent years, and now the breakdown of public company directorship numbers remains largely consistent with prior years. Men now serve on 1.42 boards on average and women serve on 1.62 boards on average, in line with last year's numbers. Egon Durban, co-CEO of investment firm Silver Lake, failed to receive majority support from shareholders of Twitter, likely due to his excessive board commitments.

Russell 3000 Directors with Significant Board Commitments

- Gregory Maffei (10)
- Ali Behbahani (10)
- Edward Mathers (9)
- Adam Portnoy (8)
- Egon Durban (7)
- Carl Gordon (7)
- Andrew Heyer (7)
- Michael Klein (7)
- Kush Parmar (7)
- Steven Rubin (7)
- Merline Saintil (7)
- Daniel Shribman (7)
- Barry Sternlicht (7)
- HSIEH Chi-Chia (7)
- MIAU Feng-Chiang (7)

Russell 3000 Board Gender (Im)Balance

Russell 3000 First Year Appointments

Gender diversity on Russell 3000 boards continues to increase despite a slight drop in the proportion of women among first year appointments. This may indicate that men retiring from boards impacted gender balance more than the appointment of women directors in 2022.

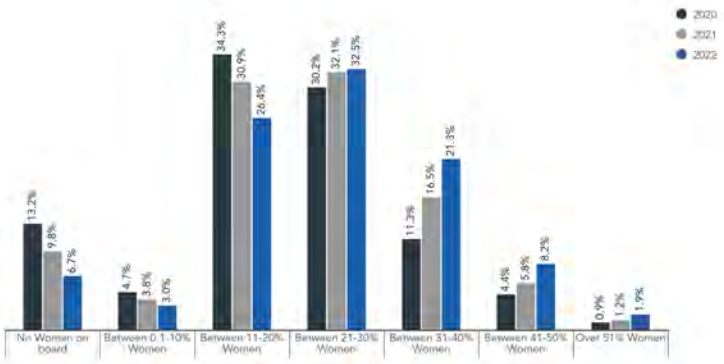
Majority-Women Boards in the S&P 500 Index*:

- Organon & Co.
- Intercontinental Exchange, Inc.
- Omnicom Group Inc.
- Citigroup Inc.
- Paramount Global
- American Water Works Company, Inc.
- Hasbro, Inc.

**Only reflects companies that held meetings during the 2022 proxy season*

GLASS LEWIS

How Many Women Serve on the Board

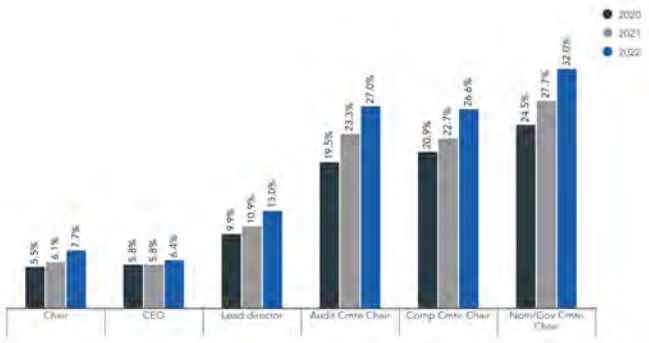


For the second consecutive year we saw a significant increase in boards with between 31-40% women. From 2020 to 2022 the number of companies with between 31-40% women serving on the board jumped approximately 10%. Several factors may be contributing to this increase in board gender diversity, including state and exchange gender diversity requirements along with investor voting policies.

Beginning in 2023, Glass Lewis will be looking for boards within the Russell 3000 to have at least 30% gender diversity. During the recent proxy season, around 1,400 boards within the Russell 3000 were below 30% gender diversity as of their annual meeting.

GLASS LEWIS

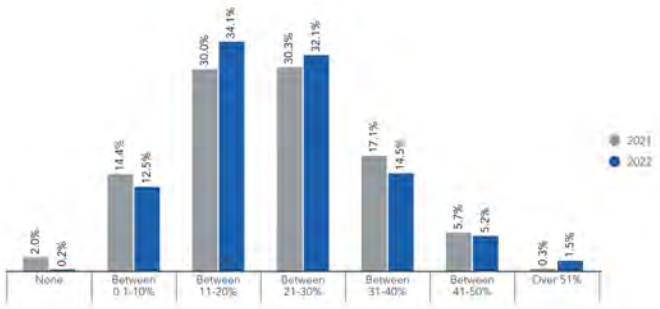
Gender (Im)Balance - Women in Board Leadership Positions



The number of women serving in board leadership positions remains strikingly low when compared to men; however, we saw notable increases in women serving in chair and lead director roles. After a particularly stagnant period from 2020 to 2021, we saw a minimal improvement in women serving in CEO roles. However, gender parity among board and company leadership positions remains well below 50%.

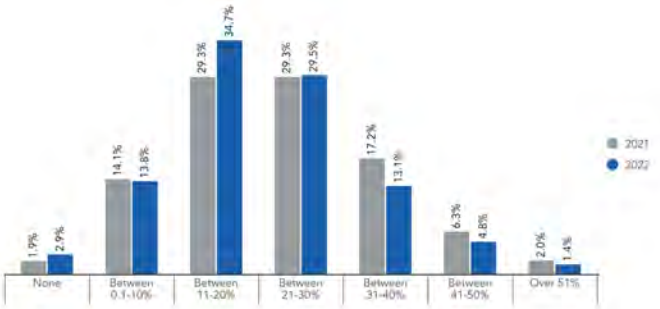
GLASS LEWIS

S&P 500: Board Racial/Ethnic Diversity Breakdown



More than 80% of S&P 500 boards in our coverage that disclosed demographic information had between 11-40% racial/ethnic diversity. Average racial/ethnic diversity was 23.4% for S&P 500 boards and 22.1% for Russell 1000 boards in 2022.

Russell 1000: Board Racial/Ethnic Diversity Breakdown



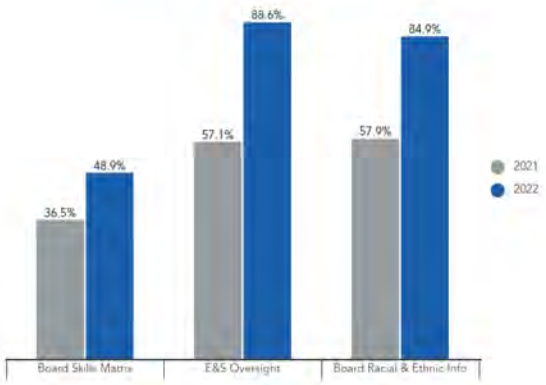
GLASS LEWIS

Governance & Disclosure Trends

Key Findings

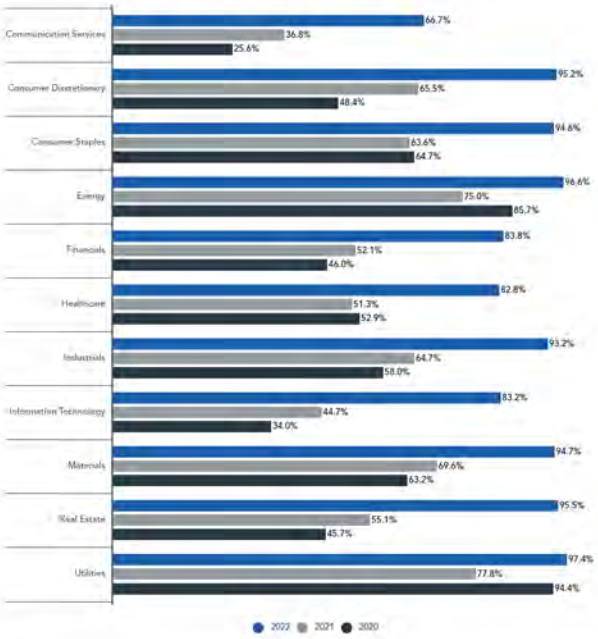
- Trends in the disclosure of board racial and ethnic diversity information has flipped in recent years, with approximately 95% of S&P 500 boards disclosing racial/ethnic diversity at either the aggregate (54%) or individual (41%) level this year compared with nearly 50% of boards that disclosed no diversity metrics just two years ago. This disclosure now represents market practice among S&P 500 companies.
- Most companies proposing amendments to their bylaws are moving towards good governance practices. Bylaw amendments to eliminate supermajority provisions and repeal classified boards again topped our list of the most common bylaw amendment proposals.

Russell 1000 Disclosure Trends



GLASS LEWIS

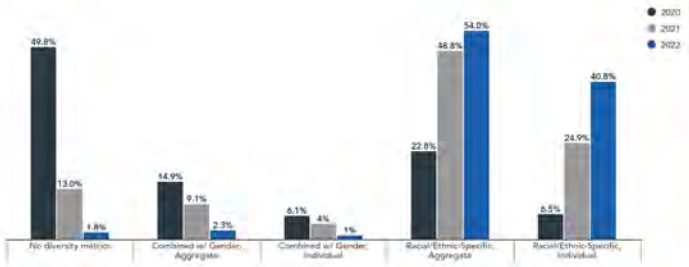
Russell 1000 E&S Oversight by Sector



Disclosure surpassed 90% in seven of the eleven GICS sectors. Communications services companies continue to severely lag other sectors, however, disclosure from these companies increased nearly 30% in 2022. We saw the most significant increase in disclosure year-over-year from real estate companies, with 40% more companies in this sector disclosing board-level E&S oversight compared with 2021.

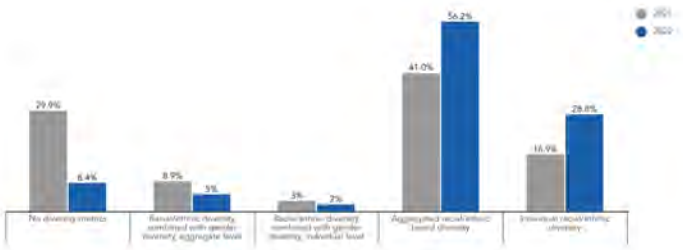
GLASS LEWIS

S&P 500 Racial/Ethnic Diversity Disclosure



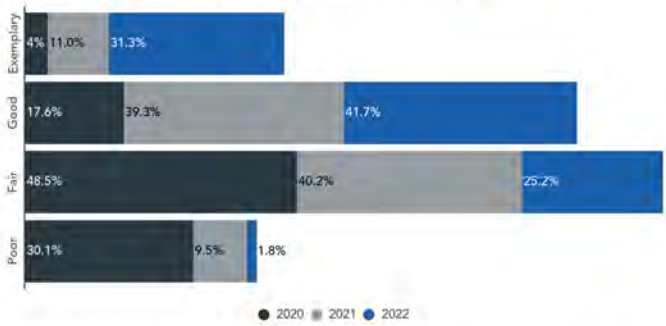
We have tracked racial/ethnic diversity disclosure within the S&P 500 since 2020 and within the Russell 1000 since 2021. In the past, almost no companies disclosed this information for the board of directors. Disclosure has increased considerably in recent years, driven by changing investor expectations along with various state and exchange disclosure requirements. Approximately 5.2% of S&P 500 boards in our coverage did not disclose the racial/ethnic diversity of directors at the aggregate or individual director level.

Russell 1000 Racial/Ethnic Diversity Disclosure



GLASS LEWIS

S&P 500 Diversity Disclosure Ratings

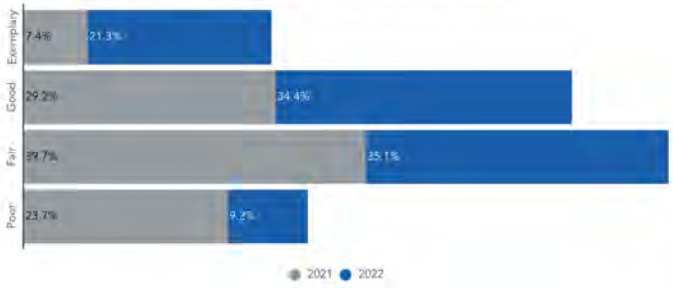


As diversity disclosure among S&P 500 companies continues to become more robust, nearly three times more S&P 500 companies received an exemplary diversity disclosure rating from Glass Lewis compared to a year ago.

We began tracking this information for S&P 500 companies in 2020 and for Russell 1000 companies in 2021. Accordingly, we have three years of data for the S&P 500 and two years of data for the Russell 1000.

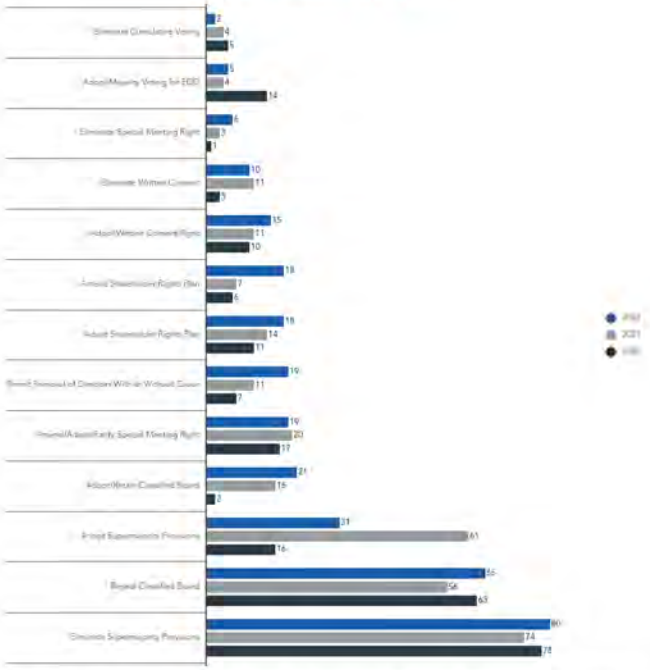
While most companies in both indices received good or fair ratings, S&P 500 companies were more likely to provide exemplary disclosure, and Russell 1000 companies were more likely to provide poor disclosure.

Russell 1000 Diversity Disclosure Ratings



GLASS LEWIS

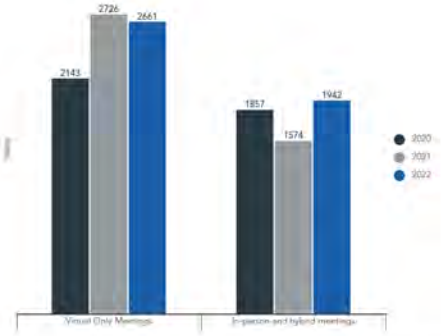
Bylaw Proposals by Type



During the 2022 proxy season we observed a significant increase in the number of management proposals to adopt or amend shareholder rights plans. While the COVID-19 pandemic caused many companies to adopt shareholder rights plans without shareholder approval, in 2022 we saw more of these proposals on annual meeting ballots. Significant market disruption and declines in valuations could be leading more companies to adopt shareholder rights plans and put them up for shareholder approval. Notably, we saw a significant decrease in proposals to adopt supermajority provisions. We also observed an increase in companies adopting classified boards – however, the number of companies with management proposals to repeal classified boards continues to outpace those adopting or retaining classified board structures.

GLASS LEWIS

Shareholder Meetings by Type



While around 400 companies returned to in-person meetings compared to a year ago, the vast majority of companies in our coverage continued to hold virtual only shareholder meetings in 2022.

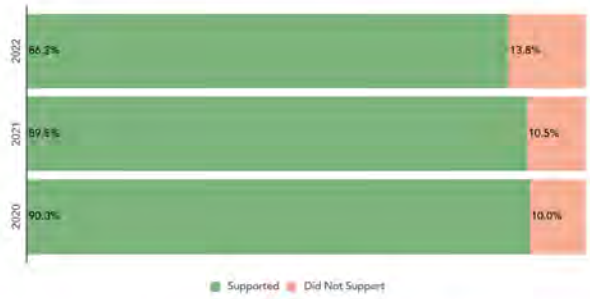
GLASS LEWIS

Election of Directors

Key Findings

- The 2022 proxy season saw an increase in the number of rejected resignations and a corresponding drop in directors leaving boards after failing to receive majority support. This trend of failed directors remaining on boards may lead some investors to reevaluate majority voting standards, and perhaps urge companies away from resignation policies and toward "true" majority voting standards.
- After falling out of our top ten last year, board gender diversity concerns were again one of our most common withhold reasons during the 2022 proxy season. As investors continue to raise the bar on board gender diversity, we expect this to continue to be an area of focus in the coming years.
- IPO governance concerns remain our top withhold reason in 2022, as it was in the previous year. We continued to observe companies entering public markets with governance practices unfavorable for shareholders, including classified boards and multi-class share structures.

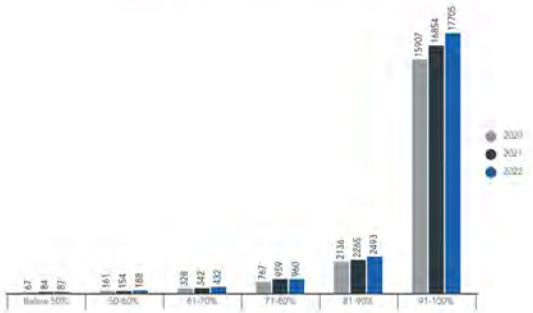
Glass Lewis Director Recommendations



Glass Lewis supported fewer directors than in recent years, reflecting policy changes taking effect for the 2022 proxy season, as well as concerns regarding board diversity, multi-class shares structures, and an increase in IPOs with poor governance.

GLASS LEWIS

Shareholder Support Levels for Directors



On average, directors received **94.2%** support from shareholders in 2022. While we continue to see increases in the number of directors falling into the sub-70% support brackets, overall shareholder support remains extremely strong.

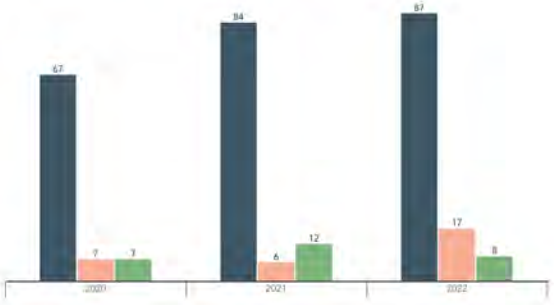
Election Methods at Companies with Failed Directors

Election Method	Number of Companies	% Discussed Results	% Directors Departed Board
Plurality	39	12.8%	0.0%
Majority	4	75.0%	50.0%*
Resignation Policy	14	79.0%	28.6%**

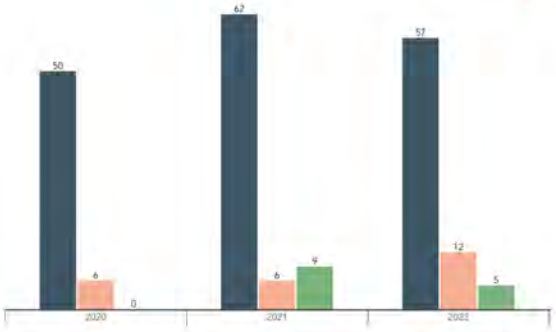
**One director will continue to serve as a director until their successor is duly elected and qualified.*
***One resignation not effective until December 31, 2022.*

GLASS LEWIS

Total U.S. Coverage Failed Directors

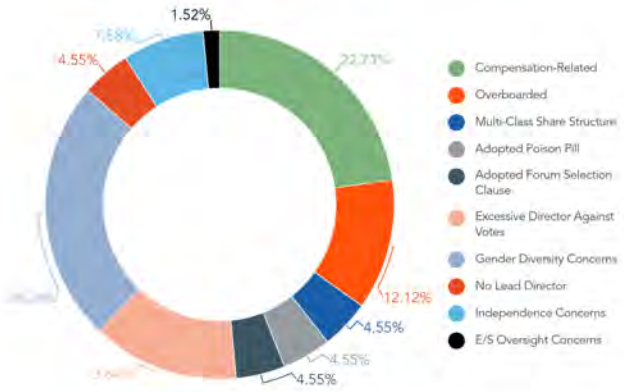


Russell 3000 Failed Directors



GLASS LEWIS

Most Common Drivers of Majority Opposition to Directors

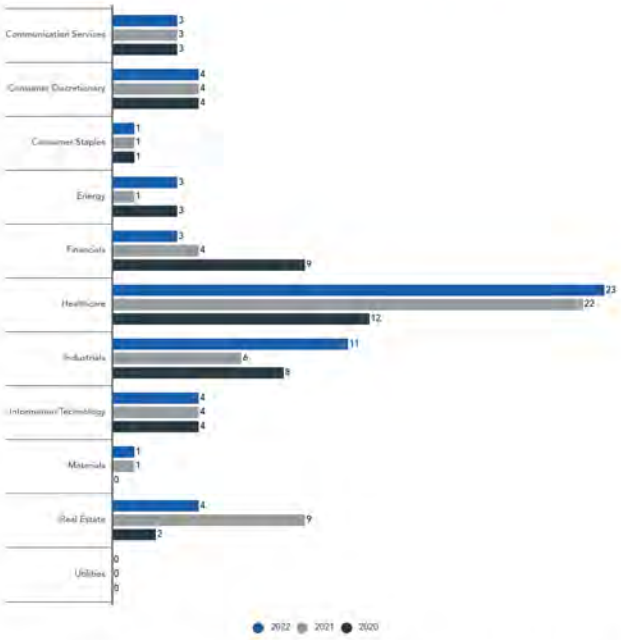


Gender diversity concerns were the most common driver of majority opposition to directors in our coverage during the past proxy season. Increased shareholder expectations and new voting policies taking effect likely contributed. Eleven of the twelve companies where gender diversity concerns drove majority opposition had zero or one woman on the board.

Poor pay practices and ongoing compensation concerns continue to drive shareholder opposition to directors. Consecutive years of low shareholder support for the compensation program and an insufficient board response can lead shareholders to go beyond simply voting against the say-on-pay proposal, and target compensation committee members directly.

GLASS LEWIS

Companies with Failed Directors by Sector



Directors at healthcare companies continue to be the target of shareholder opposition. The sector, which includes biotechnology and pharmaceuticals, has been targeted due to ongoing governance concerns likely caused by the polarizing nature of these industries.

Concerns over gender diversity and excessive compensation were the most common driver of shareholder opposition to directors at companies in the industrials sector.

These two sectors were the only two that saw increases in the number of companies with failed directors compared to last year, while all other sectors saw decreases or remained consistent with 2021.

GLASS LEWIS

Top 10 Glass Lewis Director Withhold Reasons for 2020-2022

2020	2021	2022
1. Affiliate/Insider on Cmte	1. IPO Governance Concerns	1. IPO Governance Concerns
2. No Lead Director	2. No Lead Director	2. Board Gender Diversity
3. Board Independence	3. Affiliate/Insider on Cmte	3. No Lead Director
4. IPO Governance Concerns	4. Board Independence	4. Affiliate/Insider on Cmte
5. Overboarding	5. Overboarding	5. Board Independence
6. Board Gender Diversity	6. Adoption of Exclusive Forum	6. Multi-Class Share Structure
7. Related Party Transactions	7. Related Party Transactions	7. Overboarding
8. Compensation Concerns	8. Virtual Meeting Participation	8. Vote Results Not Disclosed
9. Attendance	9. Compensation Concerns	9. Related Party Transactions
10. CFO on Board	10. CFO on Board	10. CFO on Board

IPO governance concerns remain our top reason for withholding support from directors in 2022 as we continue to see companies enter public markets with governance practices unfavorable for shareholders, including classified boards and multi-class share structures.

After falling out of our top ten last year, board gender diversity concerns were again one of our most common withhold reasons during the 2022 proxy season. As investors continue to raise the bar on board gender diversity, we expect this to continue to be an area of focus in the coming years.

Further, while ESG and diversity remain top of mind for shareholders, issues related to board independence continue to lead us to recommend against many directors. Greater board independence could help drive changes inside corporate boardrooms and lead to better governance of all issues of importance to shareholders.

GLASS LEWIS

Compensation Proposals

Key Findings

- Echoing last year's results, excessive granting and compensation remained the top issue of concern driving negative recommendations on say-on-pay proposals. Mega-grants are becoming a familiar practice within the wave of new listings, and a frequent topic of shareholder concern.
- Retention awards saw a significant uptick compared to previous years, increasing approximately 38% compared to 2021 and 61% compared to 2020. Many companies cited a highly competitive market driving the need to retain top talent.
- The number of failed golden parachute proposals doubled from 2021 and 2020 figures. Shareholders took issue with poor practices such as excessive single-trigger payments, concerning compensation arrangements for continuing executives, high overall payouts and new excise tax gross-ups.

U.S. Say-on-Pay (SOP)

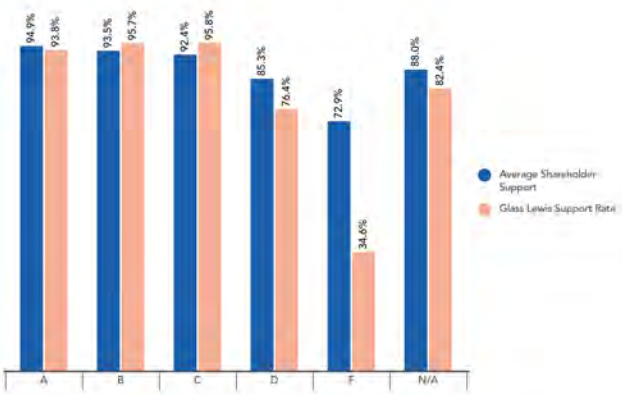
	2020	2021	2022
Total US SOP Fails	58	64	80
Total S&P 500 Fails	9	17	19
% of Failed US SOP Votes	2.30%	2.5%	3.0%
US SOP with Low Support (50-75%)	223	175	242
S&P 500 with Low Support (50-75%)	30	25	33
Avg. Shareholder Support Rate Across All US SOP	89.7%	90.0%	88.9%
GL Against Rate for All US SOP	15.7%	14.3%	15.7%
GL Against Rate for All Failed US SOP	69.0%	84.4%	73.8%
GL Against Rate for S&P 500 SOP	12.4%	11.6%	13.1%

A 20% increase in total say-on-pay fails compared to 2021 combined with an all-time high of 19 S&P 500 fails indicate a season colored with shareholder ire. Moreover, the number of companies with substantial shareholder dissent also grew approximately 38% from 2021. These results indicate that many companies may not have responded appropriately in their executive pay decisions amid a rapidly evolving economic climate and supply chain shortages.

Of the S&P 500 companies that failed their say-on-pay, the majority were from the consumer discretionary sector, including four in the hotel, restaurant and leisure industry, and information technology sectors. Approximately 63% of the S&P 500 fails were driven by excessive compensation and granting practices.

GLASS LEWIS

Support Rates by Glass Lewis Pay-for-Performance Grade



GLASS LEWIS

S&P 500 Say-on-Pay Fails

Company	2022 Support	Prior Year	P4P	GL Rec.	Excessive Granting/ Cumg	P4P Disconnect	Poor Overall Design/ Disclosure	Insufficient Response to Shareholder Dissent	Other Concerning Pay Practices
Booking Holdings Inc. (BKNG)	31.7%	90.9%	B	Against	X				
Centene Corporation (CNC)	33.6%	62.2%	F	Against	X	X		X	
CenterPoint Energy, Inc. (CNP)	22.1%	76.5%	F	Against	X	X		X	
CME Group Inc. (CME)	23.2%	90.2%	D	For	X				
D.R. Horton, Inc. (DHI)	27.4%	79.7%	D	Against	X		X		
Enphase Energy, Inc. (ENPH)	47.4%	92.8%	C	For	X		X		
FLEETCOR Technologies, Inc. (FLT)	35.6%	97.4%	F	Against	X		X		
Global Payments Inc. (GPN)	41.1%	94.9%	N/A	Against	X				
Halliburton Company (HAL)	46.2%	46.2%	D	Against		X			
Intel Corporation (INTC)	33.9%	38.1%	F	For	X	X			
JPMorgan Chase & Co. (JPM)	31.0%	90.1%	D	Against	X	X			
Netflix, Inc. (NFLX)	26.9%	50.6%	C	Against			X	X	
Norwegian Cruise Line Holdings Ltd. (NCLH)	15.3%	16.4%	F	Against		X			
Paycom Software, Inc. (PAYC)	49.2%	30.2%	D	Against				X	
Penn National Gaming Inc. (PENN)	41.8%	88.3%	D	Against	X				
ServiceNow, Inc. (NOW)	35.0%	86.5%	F	Against	X				
The TJX Companies, Inc. (TJX)	48.2%	88.5%	D	For		X			X
Ventas, Inc. (VTR)	48.9%	85.5%	F	For		X			
Wynn Resorts, Limited (WYNN)	48.5%	63.9%	N/A	Against				X	X

Keeping Up with the Joneses

Excessive granting practices continued to be the common denominator for many S&P 500 say-on-pay failures, possibly driven by other companies granting significant awards, spiraling total pay. For most companies, excessive pay stemmed from one-time awards. JPMorgan, Booking Holdings, CenterPoint, Centene and CME Group granted substantial retention awards, promotion awards, severance benefits and/or employment agreement extension awards. Global Payments saw its CEO's total reported compensation 2022 increase approximately 50% from the previous year, partially due to one-time retention awards that pushed pay above the median of Glass Lewis peers.

ServiceNow and Penn National Gaming granted discretionary awards tied to stock price hurdles, and revenue or relative TSR, respectively. The value of these awards not only exceeded the median of their self-disclosed peer groups and Glass Lewis peers, but also more than doubled their CEOs' regular pay levels.

While D.R. Horton did not make any one-time awards, its pay structure allows for potentially excessive total compensation levels via the short-term incentive plan. Cash bonuses are capped at $10 million for the chair and CEO, but any amounts earned in excess can be paid in common stock, without limit. Similarly, FLEETCOR granted front-loaded long-term incentives rather than one-time awards. However, the annualized value of these awards surpassed the median of Glass Lewis peers while also maintaining significant structural concerns.

Total compensation for the CEO of Enphase increased more than two-fold year-over-year, but the company's proxy statement didn't include a clear explanation of the rationale, or of the incentive plan structure. While the company disclosed additional information in a supplementary filing in the final days before the annual meeting date, shareholders were not swayed to support the proposal.

Intel made headlines with an aggregate CEO sign-on package that it values at $110 million (Glass Lewis estimated the approximate value to be $350 million). The award led to back-to-back say-on-pay failures in 2021 and 2022. Despite extensive outreach efforts, it does not appear shareholders were convinced.

Disconnected

After engaging with shareholders following say-on-pay failures last year, Halliburton and Norwegian Cruise Lines once again failed to impress with their response as persistent disconnects between pay and performance lingered.

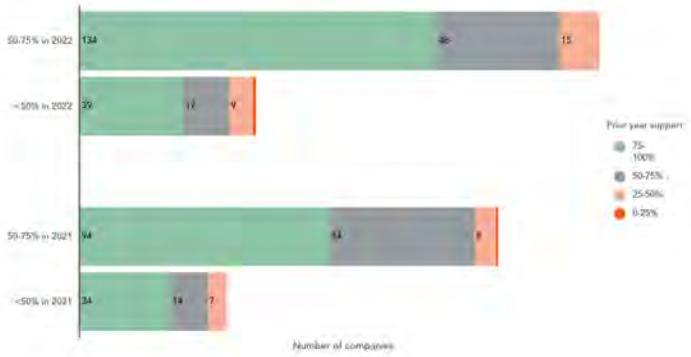
TJX Companies sustained a "D" grade that, when coupled with COVID-19 related adjustments, invited shareholder ire. Ventas underwent a proxy contest. While the dissident did not recommend an opinion for the say-on-pay proposal, it did state that it would vote its shares against the company's executive pay program. Ventas granted retention awards and substantially increased CEO pay but promised pay reductions in future years; however, those good intentions were not enough to assuage shareholder concerns.

Wrath of the Shareholders Pt. 2

Paycom had its third consecutive say-on-pay failure after insufficiently addressing shareholder concerns about a 2020 CEO mega-grant. Netflix and Wynn Resorts received low support last year and similarly provided poor responses to shareholder dissent. Despite opposition in 2021, Netflix held fast to its poorly designed compensation program structure, and Wynn Resorts proceeded to *reduce* the proportion of its LTI awards that are subject to performance conditions.

GLASS LEWIS

Failed SOPs: Prior Year Support



Generally, companies will respond to low support by addressing problems brought up through shareholder outreach efforts, attempting to ensure higher support levels in the next year. However, there was an approximate 43% increase in repeat say-on-pay failures in 2022 compared to 2021, indicating that more companies may not be responding sufficiently to shareholder dissent.

Of the SOP failures this year, 19 were at S&P 500 companies. Of those, nine had received less than 80% support back in 2021. That's a surprising number — generally, S&P 500 companies are the most likely to sufficiently respond to shareholder dissent given their role in the public eye.

This rise in repeated opposition could be driven by failure due to one-off practices in 2021 and an absence of robust commitments going forward.

GLASS LEWIS

Top Drivers of Glass Lewis Against SOP Recommendations*

2020		2021		2022	
P4P Disconnect	42.5%	Concerning Pay Practices (Excessive Grants)	22.7%	Concerning Pay Practices (Excessive Grants)	41.6%
Concerning Pay Practices (Other)	23.9%	P4P Disconnect	21.4%	Structural Concerns	34.9%
Concerning Pay Practices (Excessive Grants)	11.3%	Structural Concerns	21.4%	P4P Disconnect	34.7%
Structural Concerns	11.1%	Concerning Pay Practices (Other)	15.0%	Concerning Pay Practices (Other)	16.7%
Insufficient Response to Shareholders	9.1%	Insufficient Response to Shareholders	14.2%	Insufficient Response to Shareholders	15.8%

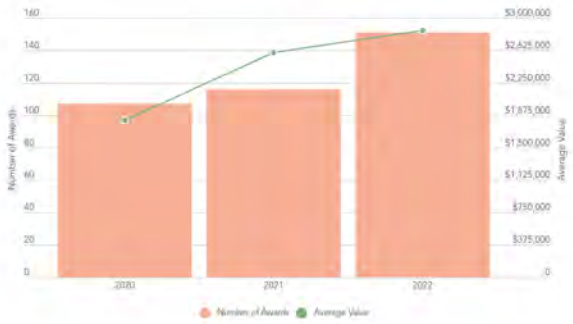
Multiple reasons may be flagged for one AGAINST recommendation. Percentages are not intended to sum to 100%. List of specific reasons are not exhaustive.

Similar to 2021, excessive grants and compensation took the top seed for say-on-pay "against" recommendation drivers. Rather than an elevated number of discretionary awards, as seen in 2021 compared to 2020, the 2022 year saw 38% increase in the number of retention one-time awards granted.

As shown in Figure 4.3 below, the rising number of retention awards was accompanied by an increase in average values for such awards among S&P 500 companies. Moreover, 2022 saw larger grants for most categories than in prior years: as displayed on Figures 4.4 and 4.5, the largest single retention award, sign-on award, discretionary award, and promotion award for 2022 exceeded the largest for 2021 or 2020.

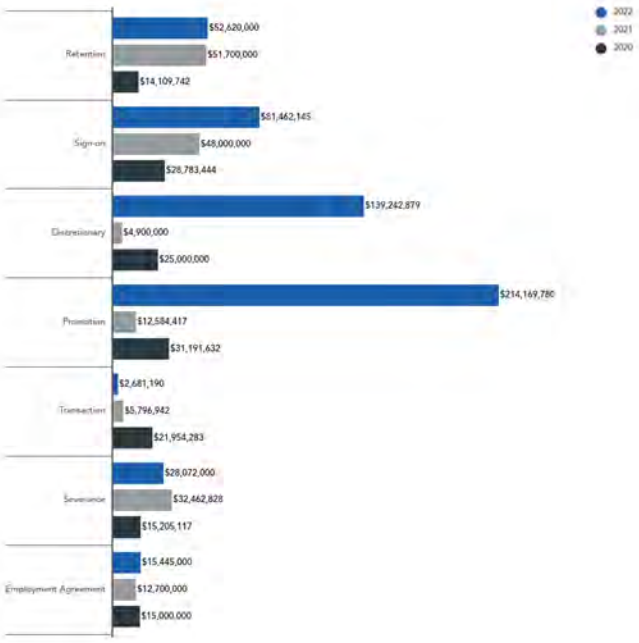
GLASS LEWIS

Retention Awards: Average Value vs. Number of Awards Granted (S&P 500)



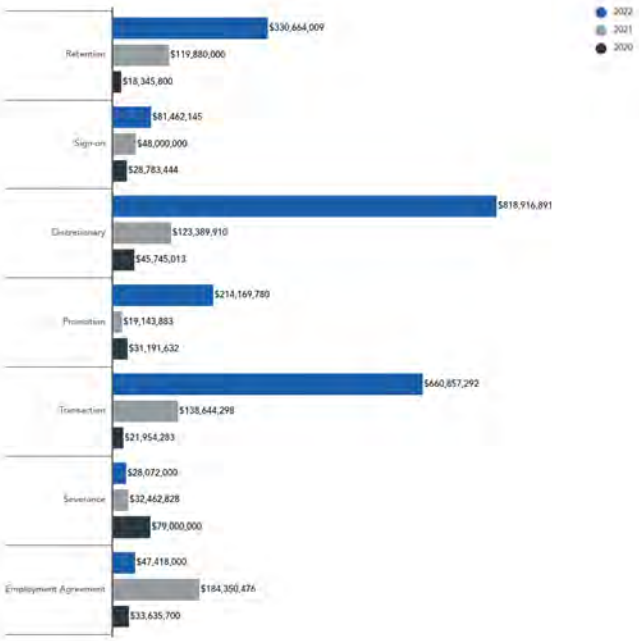
GLASS LEWIS

Highest Value One-Time Awards in S&P 500



GLASS LEWIS

Highest Value One-Time Awards Overall



GLASS LEWIS

Top Drivers of Glass Lewis Against Equity Recommendations*

2020		2021		2022	
Repricing/Buyout Provisions	40.1%	Evergreen Provision	50.8%	Evergreen	44.7%
Evergreen Provision	37.7%	Repricing/Buyout Provision	18.7%	Repricing/Buyout Provisions	27.3%
Plan Cost	22.8%	Plan Cost	9.7%	Pace of Grants	12.4%
Pace of Grants	14.8%	Excessively Dilutive	7.5%	Plan Cost	13.0%
Excessively Dilutive	10.5%	Overhang	7.5%	Excessively Dilutive	6.8%

**Multiple reasons may be flagged for one AGAINST recommendation. Percentages are not intended to sum to 100%. List of specific issues is not exhaustive.*

Pace of granting history made a comeback into the top five list for Glass Lewis equity plan against recommendations in 2022. This likely reflects the excessive compensation and granting practices outlined above, but it could also have been impacted by decreasing stock prices during the pandemic, leading to the granting of more shares for the same amount of pay.

GLASS LEWIS

Other Compensation Proposals

Equity Plans	2020	2021	2022
Average Shareholder Support Rate	87.7%	88.0%	87.5%
Glass Lewis Support Rate	77.9%	76.4%	85.7%
Number of Failed Proposals	11 (1.4%)	9 (1.0%)	7 (0.9%)
Number with Significant Opposition (25% to 50%)	112 (14.4%)	121 (14.1%)	112 (14.9%)

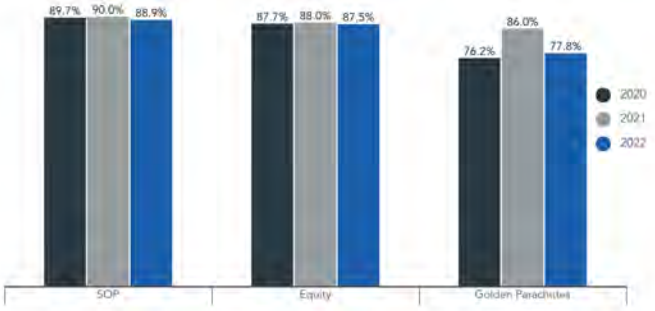
Director Compensation	2020	2021	2022
Average Shareholder Support Rate	90.1%	94.8%	90.6%
Glass Lewis Support Rate	87.9%	84.0%	93.1%
Number of Failed Proposals	0 (0%)	0 (0%)	2 (6.9%)
Number with Significant Opposition (25% to 50%)	3 (0.75%)	1 (2.9%)	0 (0%)

Golden Parachutes	2020	2021	2022
Average Shareholder Support Rate	76.2%	86.0%	77.8%
Glass Lewis Support Rate	63.5%	84.0%	71.8%
Number of Failed Proposals	6 (11.8%)	5 (6.3%)	11 (15.5%)
Number with Significant Opposition (25% to 50%)	14 (27.5%)	7 (8.9%)	14 (19.7%)

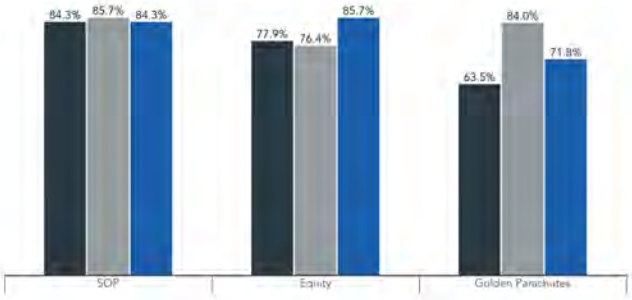
While the number of equity plan fails may be decreasing year-over-year, 2022 saw two director compensation plans fails, up from zero in the two prior years. Director compensation has received more attention in recent years, particularly among biotechnology companies. Some companies faced lawsuits from shareholders citing excessive compensation, and some of the plans being up for vote were proposed to satisfy the settlement of these suits.

GLASS LEWIS

Average Shareholder Support Rate



Glass Lewis Support Rate



Golden parachutes support rates are notoriously variable as these proposals depend greatly on what is negotiated during merger discussions. We saw a substantial increase in the number of failed golden parachutes this season, as indicated in Table 4.5, with 11 failures in 2022 compared to 5 in 2021 and 6 in 2020. All of these companies featured one or more of the following practices not in shareholder interest: excessive single-trigger arrangements, high payout levels, newly added excise tax gross-ups, and/or concerning compensation arrangements following the merger.

GLASS LEWIS

Average CEO Compensation*

S&P 500 CEO Direct Compensation*	2020	2021	2022
Average	$14,605,435.17	$16,500,347.71	$19,298,429.77
Median	$12,474,037.43	$12,451,300.18	$15,072,293.48
Highest	$249,904,602.32 (Google)	$702,000,886.00 (Paycom)	$329,595,305.16 (Intel)

All CEO Direct Compensation*	2020	2021	2022
Average	$5,801,095.87	$5,882,319.40	$7,075,085.76
Median	$3,436,519.85	$3,606,086.82	$4,324,250.32
Highest	$249,904,602.32 (Google)	$702,000,886.00 (Paycom)	$718,434,522.56 (The Trade Desk)

**Based on Glass Lewis' pay-for-performance valuation methodology.*

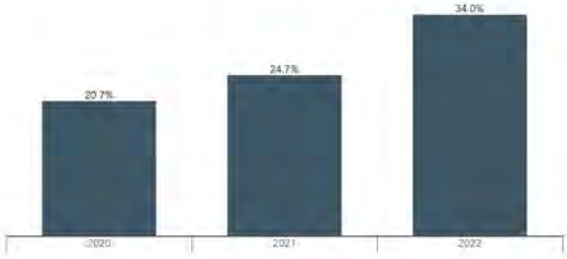
CEO pay levels continue to rise despite market tumult. Indeed, the year-over-year increase in average and median CEO pay for the S&P 500 was approximately 17% and 21%, respectively, between 2022 and 2021, compared to just 13% and 0% between 2021 and 2020. This is driven by a multitude of factors such as the increasing use of mega-grants, retention concerns and resulting one-time awards, and payouts determined after a successful navigation through the COVID-19 pandemic and supply chain shortages.

Best Practices

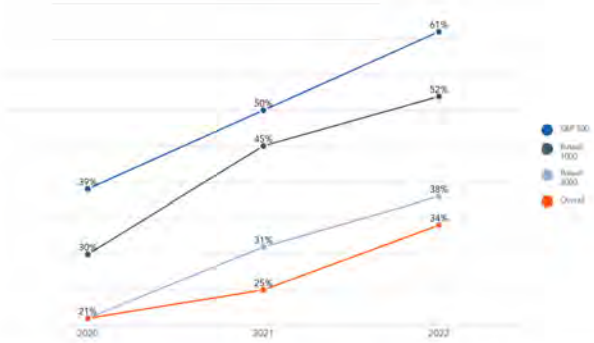
	2020	2021	2022
Clawback	74.4%	76.3%	75.3%
Ownership Guidelines	75.2%	75.7%	75.2%
Anti-Hedging Policy	88.8%	92.2%	94.8%
Single-Trigger Provisions	30.6%	27.3%	23.9%
Legacy?	25.3%	24.1%	22.8%
Excise Tax Gross-Ups	8.8%	7.5%	6.5%
Legacy?	61.7%	71.0%	72.8%

GLASS LEWIS

E&S Metric Inclusion in Incentive Plans



E&S Metric Inclusion by Index



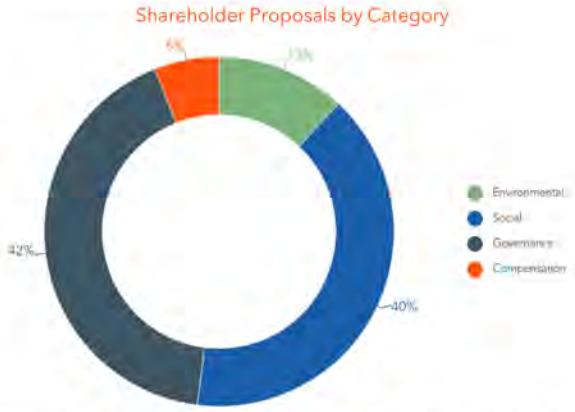
Quickly developing into a common market practice, a majority of S&P 500 and Russell 1000 companies have adopted an E&S metric in one of their incentive plans. The majority of E&S metrics related to human capital management and diversity. As the practice continues to become more widespread, the onus falls on companies to provide better disclosure of how E&S performance is assessed and how it impacted payouts.

GLASS LEWIS

Shareholder Proposals

Key Findings

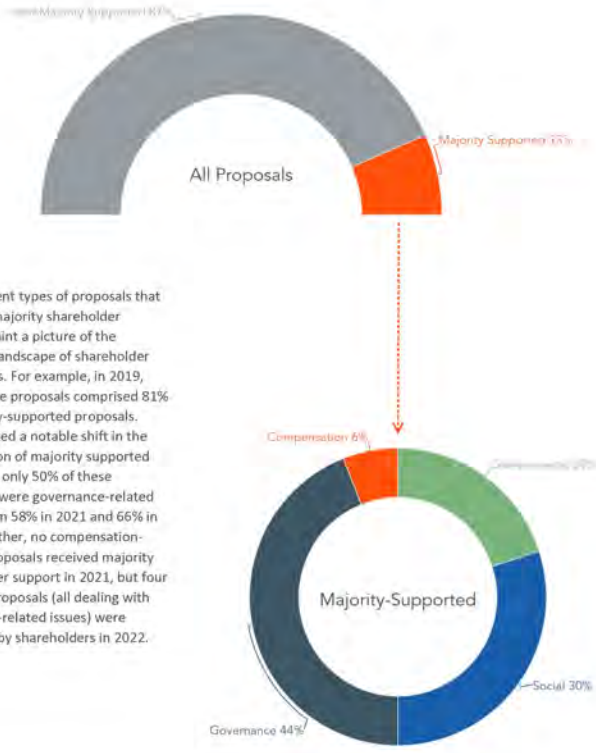
- As a result of more permissive SEC rules, and the growing momentum around environmental and social issues, there was a roughly 30% increase in the number of shareholder proposals that went to a vote on a year-over-year basis, which included approximately 100 more environmental and/or social proposals than in the previous year
- There was a 400% increase in the number of anti-ESG proposals that went to a vote in 2022. These proposals often take the form of more traditional proposals but are implicitly aimed at rolling back companies' environmental and social initiatives
- Technology companies continue to be a significant focus for investors, and have consistently received the highest number of shareholder proposals. Between three companies (Meta Platforms, Alphabet, and Amazon.com), shareholders voted on almost 150 shareholder proposals over the last four years, with 44 of these proposals going to a vote in 2021.



For the first time in recent memory, governance proposals did not make up the majority of proposals submitted to a vote during the 2022 proxy season. Following investors' increasing scrutiny on how companies are managing ESG issues, environmental and social proposals outnumbered governance proposals, with the most significant increase in the number of social proposals that went to a vote. This figure nearly doubled on a year-over-year basis, with 209 such proposals being featured on corporate ballots, up from just 117 the prior year.

GLASS LEWIS

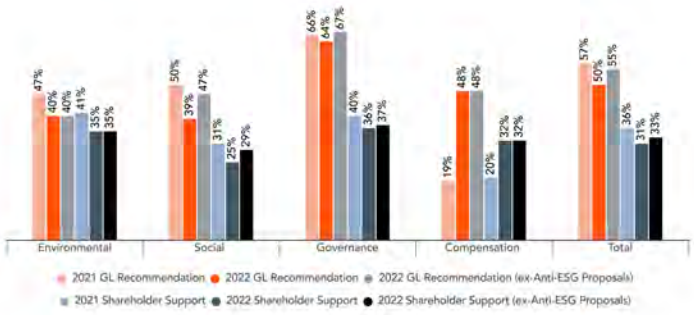
Majority Supported Shareholder Proposals



The different types of proposals that received majority shareholder support paint a picture of the changing landscape of shareholder resolutions. For example, in 2019, governance proposals comprised 81% of majority-supported proposals. 2022 marked a notable shift in the composition of majority supported proposals; only 50% of these proposals were governance-related (down from 58% in 2021 and 66% in 2020). Further, no compensation-related proposals received majority shareholder support in 2021, but four of these proposals (all dealing with severance-related issues) were approved by shareholders in 2022.

GLASS LEWIS

Shareholder Support vs. Glass Lewis Recommendations



Although there were far more proposals that went to a vote in 2022, shareholder support for these proposals dropped on a year-over-year basis, as did the number of proposals for which we recommended in favor. While some of this can be explained by the significant increase in anti-ESG proposals, that does not explain most of this decline. Nor do we believe that it is explained by a change in how Glass Lewis or investors consider ESG-related issues.

Rather, our contention is that the quality and targeting of proposals was diminished in 2022, potentially as a result of the SEC permitting more proposals to make it to a vote. As example of the decrease in the quality of these proposals, the number of environmental and social proposals that touch on financially material topics as defined by the Sustainability Accounting Standards Board ("SASB") framework was nearly halved on a year-over-year basis. While nearly two-thirds (64%) of environmental and social proposals were financially material in 2021, that number dropped significantly to just over one-third (36%) during the 2022 proxy season.

Notable Meetings

Director and Compensation Failures

Arrowhead Pharmaceuticals, Inc. (ARWR) March 17, 2022

- *Election of Mauro Ferrari* — *35% support/ 65% opposition*
- *Election of William Waddill* — *37% support/ 63% opposition*
- *Election of Michael S. Perry* — *42% support/ 58% opposition*
- *Advisory Vote on Executive Compensation* — *20% support/ 80% opposition*
- *Approval of NED Compensation Policy* — *23% support/ 77% opposition*

Arrowhead's problematic executive and director compensation practices continued to drive shareholder opposition at the 2022 annual meeting. Executive compensation concerns centered on the potentially excessive nature of the CEO's equity grants, further compounded by the award structure. Additionally, the non-executive director compensation policy was put up for vote as result of a lawsuit; the settlement requires the company to limit non-employee director compensation for a five-year period but the results suggest shareholders believe there is more work to do. Additionally, directors Ferrari, Waddill and Perry all failed to receive majority support. Each of these directors is a member of the board's compensation committee, indicating that shareholders are escalating their concerns with the committee's responsiveness to more directors – last year, only Waddill and Perry failed to receive majority support.

G-III Apparel Group, Ltd. (GIII) June 9, 2022

- *Election of Victor Herrero* — *40% support/ 60% opposition*
- *Election of Laura Pomerantz* — *38% support/ 62% opposition*
- *Election of Richard White* — *39% support/ 61% opposition*
- *Advisory Vote on Executive Compensation* — *22% support/ 78% opposition*

At G-III Apparel Group's 2022 annual meeting, shareholders expressed their concerns with the company's executive compensation program for the third consecutive year. Despite some improvements to the compensation program in response to low shareholder voting support, pay during fiscal year 2022 remained substantial relative to both peers, and to the company's own pre-COVID levels. Within the context of low TSR performance and the repeated misalignment between pay and performance, CEO payouts continued to drive shareholder opposition at the 2022 Annual Meeting. In addition, directors White and Pomerantz, each a member of the compensation committee, failed to receive majority support from shareholders, a further indication of shareholder discontent with the committee's responsiveness to the ongoing compensation concerns. Meanwhile, director Herrero also failed to receive majority support, suggesting that shareholders are dissatisfied with the scope of this director's commitments. Herro serves as CEO of Australian Securities Exchange-listed Lovisa Holdings Limited while serving on four total boards as of GIII's annual meeting.

Netflix, Inc. (NFLX) June 2, 2022

- *Election of Timothy M. Haley* — *32% support/ 68% opposition*
- *Advisory Vote on Executive Compensation* — *27% support/ 73% opposition*

While Netflix's past failures to implement majority-approved shareholder proposals resulted in long-term opposition toward its directors (this was the ninth annual meeting where at least one nominee experienced significant opposition), we note that the company took steps to rectify these concerns at the 2022 annual meeting. Specifically, the board included proposals which sought to increase shareholder rights, including the repeal of the board's classified structure and the removal of certain supermajority requirements, as well as the restoration of shareholders' rights to call special meetings. Despite these governance improvements, the company again failed to make material changes to its compensation program, which has elicited shareholder opposition for three consecutive years. Mr. Haley, the chair of the compensation committee, received high opposition this year in response to these ongoing compensation concerns.

PacWest Bancorp (PACW) May 10, 2022

- *Election of Robert A. Stine* — *49% support / 51% opposition*
- *Advisory Vote on Executive Compensation* — *20% support/ 80% opposition*

After failing to be approved for two consecutive years, PacWest Bancorp's say-on-pay received even less shareholder support in 2022. Although the company made efforts to engage with shareholders, the meetings were set against a massive, front-loaded CEO retention award, granted as part of succession planning efforts. In the end, it seems that the engagement efforts were not enough to allay shareholder concerns, likely tied to the excessive CEO retention award. Additionally, shareholders expressed their disapproval of the board's response by opposing the election of Mr. Stine, who served as chair of the compensation committee for the last two years. In response to this opposition, Mr. Stine tendered his resignation, which the board accepted and will be effective as of December 31, 2022.

Tutor Perini Corporation (TPC) May 18, 2022

- *Election of Robert C. Lieber* — *34% support/ 66% opposition*
- *Election of Michael R. Klein* — *34% support/ 66% opposition*
- *Election of Michael F. Horodniceanu* — *40% support/ 60% opposition*
- *Election of Peter Arkley* — *38% support/ 62% opposition*
- *Election of Raymond R. Oneglia* — *49% support/ 51% opposition*
- *Advisory Vote on Executive Compensation* — *31% support/ 69% opposition*

Tutor Perini's shareholders have once again voiced their concerns relating to the company's compensation plan — opposition which has been ongoing since the 2011 annual meeting. As with last year, all members of the compensation committee failed to receive majority support from shareholders, an indication of continued dissatisfaction with the compensation program. It appears that the board's reluctance to replace its failed directors is contributing to shareholder discontent, which may explain this continued high level of opposition. In addition, all members of the board's corporate governance and nominating committee failed to receive majority support from shareholders, which is likely a symptom of the company's failure to appoint additional directors

pursuant to the diversity requirements outlined under SB-826 and AB-979, which were applicable to public companies headquartered in California.

Election of Directors Protest Votes

Everbridge, Inc. (EVBG) May 19, 2022

- *Election of Bruns Grayson* — *42% support/ 58% opposition*

Since 2018, Everbridge directors have consistently received higher levels of shareholder opposition, which likely correlates to historical concerns with the company's executive compensation program and practices. However, the 2022 annual meeting is the first time one of these directors, Bruns Grayson, failed to received majority support. Interestingly, an exempt solicitation by Ancora Holdings Group, LLC, was filed in April 2022 which stated its intent to withhold from four incumbent directors, including Mr. Grayson. Among other reasons, Ancora cited capital allocation, lack of board refreshment and diversity, compensation decisions, corporate oversight, and the chair's conflicts of interest as the primary concerns. Additionally, we note that after the sudden resignation of the company's CEO in December 2021, share prices plunged. It seems likely that share price volatility, coupled with multiple ongoing governance and compensation concerns, led to deeper discontent and demand for reform.

Expedia Group, Inc. (EXPE) June 16, 2022

- *Election of Chelsea Clinton* — *50% support/ 50% opposition*
- *Election of Craig A. Jacobson* — *48% support/ 52% opposition*

Director Clinton, chair of Expedia Group's compensation committee, failed to receive majority support at the 2022 annual meeting. It appears that this opposition stems from concern surrounding the company's pay practices, specifically regarding decisions made in 2021 around CEO Peter Kern's compensation arrangements, which included massive front-loaded long-term incentive awards with a combined grant date fair value of $294.4 million. These large awards also had structural issues, namely the absence of any performance-based vesting conditions. Due to the company's triennial advisory "say-on-pay" and the fact that no compensation proposal was on ballot this year, shareholders chose to alternatively direct their discontent towards the chair of the compensation committee, director Clinton. Additionally, nominating committee chair Jacobson received significant opposition, likely in response to poor corporate governance practices, including a multi-class share structure with unequal voting rights and failure to appoint independent leadership.

Natera, Inc. (NTRA) May 25, 2022

- *Election of James Healy* — *38% support/ 62% opposition*
- *Election of Gail Marcus* — *49% support/ 51% opposition*

The members of Natera's nominating and corporate governance committee remained the subject of significant shareholder opposition at the 2022 annual meeting. This year's results appear to be symptomatic of concerns which have been ongoing since the 2019 annual meeting, where the nominating and corporate governance

committee failed to address shareholder concerns stemming from director Healy's excessive concurrent directorship commitments. This year, these concerns have been exacerbated by the board's approval of an exclusive forum provision in the company's bylaws, in addition to directors Healy's and Botha's continued service on the board following majority shareholder opposition.

Silgan Holdings Inc. (SLGN) May 31, 2022

- *Election of R. Philip Silver* — *48% support/ 52% opposition*

Director Silver failed to receive majority support at Silgan Holdings' 2022 annual meeting, suggesting shareholders disapprove of the stockholders agreement to which he is a party. Under the terms of the agreement, directors Silver and Horrigan bear the contractual right to nominate each of the directors for election, leaving little consideration for shareholder input on board composition. This, combined with the fact that the board lacks a committee to oversee director nominations, appears to have contributed to growing shareholder opposition toward directors. Silver and Horrigan over the past several annual meetings, as these governance measures enable both directors to exert outsized influence on the board's nomination process. Pursuant to the company's majority voting standard for director elections, the opposition to Mr. Silver, as detailed above, would serve as grounds for his removal from the board. The company states that it is in the process of selecting Mr. Silver's successor.

Twitter, Inc. (TWTR) May 25, 2022

- *Election of Egon Durban* — *43% support/57% opposition*

At Twitter's 2022 annual meeting, director Durban failed to receive majority support from shareholders. We believe this opposition is likely due to the number of Mr. Durban's public company commitments, as he sits on seven boards. Pursuant to the company's director resignation policy, Mr. Durban subsequently tendered his resignation, though the board has since rejected it in exchange for Mr. Durban's agreement to reduce his number of concurrent directorships to a total of five prior to next year's annual meeting. In this case, while the failed director remains on the board, it appears that the company is attempting to address its shareholders' concerns.

Universal Health Services (UHS) May 18, 2022

- *Election of Maria R. Singer* — *37% support/63% opposition*

Director Singer, a member of United Health Services' nominating and governance committee, failed to receive majority support at the company's 2022 annual meeting. This may indicate shareholder dissatisfaction with both the company's multi-class share structure, and with its lack of board-level environmental and social oversight. The result is especially notable considering that Universal Health Services is a controlled company. Due to the multi-class voting structure, only Class B and Class D common stock holders voted on director Singer's election. In our view, this result demonstrates that the company's shareholders are becoming increasingly wary of the relatively compromised voting power allotted to its Class A and Class B common stock.

GLASS LEWIS

Compensation Strikes

Norwegian Cruise Line Holdings Ltd. (NCLH) - June 16, 2022

- *Advisory Vote on Executive Compensation* *15% Support / 85% opposition*

After receiving only 16% support for its say-on-pay vote last year, the company made changes to the short- and long-term incentive plans' structures and replaced two members of the compensation committee. Despite these efforts to assuage concerns, and the lack of further one-time awards, relatively high (and increasing) regular pay levels for the CEO may have outweighed these considerations for shareholders.

Endo International plc (ENDP) - June 9, 2022

- *Advisory Vote on Executive Compensation* *15% Support / 85% opposition*

Following a low level of support for last year's say-on-pay, the company engaged with shareholders and made changes to it incentive structures. However, it does not appear that all the changes for 2022 were in line with shareholder expectations. In connection with its Prepaid 2022 Incentive Compensation Program, the company shortened vesting and performance periods, despite holding award values level. The rationale for these decisions appears to not have held water with shareholders, leading to a further decline in support for the company's compensation program.

The Goodyear Tire & Rubber Company (GT) - April 11, 2022

- *Advisory Vote on Executive Compensation* *21% Support / 79% opposition*

Against a backdrop of rising compensation levels and CEO pay that outpaced peers, as well as COVID-19 pay adjustments in 2020 that caused significant shareholder concern, the company granted substantial one-time awards to NEOs in connection with its acquisition of Cooper Tires. The combination of high pay with weak long-term TSR performance appears to have been too much for shareholders to tolerate.

CenterPoint Energy, Inc. (CNP) - April 22, 2022

- *Advisory Vote on Executive Compensation* *22% Support / 78% opposition*

The company granted significant retention awards to the CEO, as well as excessive severance payments to the former chair. While the company discussed the rationale for these awards with shareholders, their size and structure remained troubling, with the lack of performance conditions for the CEO's awards a particular sore spot. Ultimately, the company's rationale was insufficient to mollify shareholder concerns.

GLASS LEWIS

Pebblebrook Hotel Trust (PEB) - May 16, 2022

- *Advisory Vote on Executive Compensation* *25% Support / 75% Opposition*

During fiscal year 2021, the company granted substantial retention awards to executives, subject only to time-based vesting requirements. Given the quantum of these awards, the Company experienced significant disconnect between pay and performance, resulting in a dramatic decrease in historical alignment. This misalignment, heightened by off-cycle awards untethered to performance-based requirements, likely influenced the low level of shareholder support for the year in review.

Flowserve Corporation (FLS) - May 12, 2022

- *Advisory Vote on Executive Compensation* *30% Support / 70% Opposition*

Despite below target incentive payouts during fiscal year 2021, the company experienced a worsening disconnect between pay and performance. NEOs were granted substantial retention awards, amplifying pay levels and further exacerbated by the lack of any performance-based vesting requirements, likely influencing low levels of shareholder support.

GLASS LEWIS

Appendix A

Failed Directors from January to June 2022 (Glass Lewis U.S. Coverage)

Company	Voting Method	Director Name	Continues to Serve on Board?
Advaxis, Inc.	Majority w/ Resignation Policy	Elect Richard J. Berman	YES
		Elect Kenneth A. Berlin	YES
		Elect David Sidransky	YES
		Elect James P. Patton	YES
Aemetis, Inc.	Plurality	Elect Francis P. Barton	YES
Albany International Corp.	Plurality	Elect John R. Scannell	YES
Aldeyra Therapeutics, Inc.	Plurality	Elect Richard H. Douglas	YES
Arrowhead Pharmaceuticals, Inc.	Majority w/ Resignation Policy	Elect Mauro Ferrari	YES
		Elect William Waddill	YES
		Elect Michael S. Perry	YES
Ashford Hospitality Trust, Inc.	Majority w/ Resignation Policy	Elect Kamal Jafarnia	YES
Avalon Holdings Corporation	Plurality	Elect Stephen L. Gordon	YES
		Elect Kurtis D. Gramley	YES
Baudax Bio, Inc.	Plurality	Elect Winston J. Churchill	YES
		Elect Arnold Baskies	YES
Blueprint Medicines Corporation	Plurality	Elect Mark A. Goldberg	YES
Carriage Services, Inc.	Majority w/ Resignation Policy	Elect Bryan D. Leibman	NO
		Elect Achille Messac	YES
Chimerix, Inc.	Plurality	Elect Patrick Machado	YES
Clovis Oncology, Inc.	Plurality	Elect Brian G. Atwood	YES
Elanco Animal Health Inc.	Plurality	Elect Kapila K. Anand	YES
		Elect Lawrence E. Kurzius	YES
Encore Wire Corporation	Majority w/ Resignation Policy	Elect Gregory J. Fisher	YES
Everbridge, Inc.	Plurality	Elect Bruns H. Grayson	YES
Expedia Group, Inc.	Plurality	Elect Chelsea Clinton	YES
		Elect Craig A. Jacobson	YES
Frequency Therapeutics, Inc.	Plurality	Elect Robert Langer	YES

First Merchants Corporation	Plurality	Elect F. Howard Halderman	YES
Gladstone Commercial Corporation	Plurality	Elect Paul W. Adelgren	YES
Global Net Lease, Inc.	Plurality	Elect P. Sue Perrotty	YES
		Elect Lee M. Elman	YES
G-III Apparel Group, Ltd.	Plurality w/ Resignation Policy	Elect Laura H. Pomerantz	YES
		Elect Richard D. White	YES
		Elect Victor Herrero	YES
GSE Systems, Inc.	Majority	Elect Kathryn O'Connor Gardner	YES
H&E Equipment Services, Inc.	Plurality w/ Resignation Policy	Elect Lawrence C. Karlson	YES
Helix Energy Solutions Group, Inc.	Plurality w/ Resignation Policy	Elect Jan Rask	NO
Hepion Pharmaceuticals, Inc.	Plurality	Elect Timothy Block	YES
		Elect Gary S. Jacob	YES
		Elect John P. Brancaccio	YES
Heritage-Crystal Clean, Inc.	Plurality	Elect Charles E. Schalliol	YES
Iovance Biotherapeutics, Inc.	Majority	Elect Iain Dukes	YES
Ladder Capital Corp	Plurality	Elect Alan H. Fishman	YES
Lordstown Motors Corp.	Plurality w/ Resignation Policy	Elect Angela Strand	YES
Medpace Holdings, Inc.	Plurality	Elect Ashley M. Keating	YES
Mesa Air Group, Inc.	Plurality	Elect Spyridon P. Skiados	YES
Natera, Inc.	Plurality	Elect James I. Healy	YES
		Elect Gail B. Marcus	YES
Netflix, Inc.	Plurality	Elect Timothy M. Haley	YES
Neuronetics, Inc.	Plurality	Elect Bruce J. Shook	YES
Northwest Pipe Company	Plurality w/ Resignation Policy	Elect Michael C. Franson	YES
Opgen, Inc.	Plurality	Elect Oliver Schacht	YES
		Elect William E. Rhodes	YES
		Elect Mario Crovetto	YES
		Elect R. Don Elsey	YES
		Elect Prabhavathi Fernandes	YES
Otonomy, Inc.	Plurality	Elect Theodore R. Schroeder	YES
Outset Medical, Inc.	Plurality	Elect D. Keith Grossman	YES
PacWest Bancorp	Majority w/ Resignation Policy	Elect Robert A. Stine	YES*
Pluristem Therapeutics Inc.	Majority	Elect Mark Germain	NO

GLASS LEWIS

		Elect Doron Shorrer	NO
		Elect Moria Kwiat	NO
Ring Energy, Inc.	Plurality	Elect Regina Roesener	YES
Saga Communications, Inc.	Plurality	Elect Roy F. Coppedge III	YES
Servotronics, Inc.	Plurality	Elect Edward C. Cosgrove	YES
		Elect Lucion P. Gygax	YES
Silgan Holdings Inc.	Majority	Elect R. Philip Silver	YES**
Tabula Rasa HealthCare, Inc.	Plurality	Elect A. Gordon Tunstall	YES
		Elect Orsula V. Knowlton	YES
The Necessity Retail REIT, Inc.	Plurality	Elect Leslie D. Michelson	YES
TG Therapeutics, Inc.	Plurality	Elect Sagar Lonial	YES
		Elect Yann Echelard	YES
		Elect Daniel Hume	YES
TPI Composites, Inc.	Plurality	Elect Tyrone M. Jordan	YES
Tutor Perini Corporation	Plurality	Elect Michael R. Klein	YES
		Elect Robert C. Lieber	YES
		Elect Peter Arkley	YES
		Elect Michael F. Horodniceanu	YES
		Elect Raymond R. Oneglia	YES
Twist Bioscience Corporation	Plurality	Elect Nelson C. Chan	YES
Twitter, Inc.	Majority w/ Resignation Policy	Elect Egon Durban	YES
Universal Health Services, Inc.	Plurality	Elect Maria Singer	YES
Upland Software, Inc.	Plurality	Elect David D. May	YES
Vector Group Ltd.	Majority w/ Resignation Policy	Elect Stanley S. Arkin	YES
Virco Mfg. Corporation	Plurality	Elect Donald R. Rudkin	YES
Xencor, Inc.	Plurality w/ Resignation Policy	Elect Yujiro S. Hata	NO
Yext, Inc.	Elect Yujiro S. Hata	Elect Seth H. Waugh	YES

*Resignation not effective until December 31, 2022
**Will continue to serve as a director until his successor is duly nominated and qualified.

GLASS LEWIS

Appendix B

Glass Lewis Director Withhold/Against Reasons, Proxy Season 2022

Withhold/Against Reason	S&P 500	Russell 3000
Adoption of Exclusive Forum Provision	12	36
Affiliate/Insider on a Committee	16	137
Attendance	0	19
Attendance Record Disclosure Incomplete	0	7
Auditor not up for Ratification	1	25
Board Gender Diversity	11	249
CFO on Board	2	38
Director Received Excessive Against Votes	1	17
Director Serves on Excessive Audit Committees	2	10
Insufficient Board Independence	5	90
Insufficient Committee Meetings	0	8
Insufficient Response to Shareholder Dissent Regarding Compensation Issues	4	20
Interlocking Directorship	0	5
IPO Governance Concerns	0	461
Material Weakness	0	18
No Compensation Committee	0	3
No Lead Director	7	158
Ongoing Compensation Concerns	16	47
Overboarding	22	97
Poison Pill	0	3
Related Party Transactions	6	61
Restated Financial Statements	0	6
SHP Not Implemented	7	9
Virtual-only Meeting Limits Shareholder Participation	0	18
Vote Results Not Disclosed	0	11
Multi-Class Share Structure with Unequal Voting Rights	21	162
Insufficient Board Level Oversight of Environmental and Social Issues	8	8
Insufficient Diversity of Underrepresented Communities	0	10
Concerning Pay Practices	1	12

GLASS LEWIS

Appendix C

Failed Say-on-Pay Proposals

Company	Glass Lewis Recommendation	Shareholder Support
Harbor Custom Development, Inc.	For	10.0%
Norwegian Cruise Line Holdings Ltd.	Against	15.3%
Endo International plc	Against	15.3%
Upland Software, Inc.	Against	17.5%
Redwood Trust, Inc.	Against	18.9%
Pebblebrook Hotel Trust	Against	20.0%
PacWest Bancorp	Against	20.0%
Arrowhead Pharmaceuticals, Inc.	Against	20.4%
The Goodyear Tire & Rubber Company	Against	20.8%
Palomar Holdings, Inc.	Against	21.8%
CenterPoint Energy, Inc.	Against	22.1%
G-III Apparel Group, Ltd.	Against	22.5%
Flowserve Corporation	Against	23.0%
CME Group Inc.	For	23.2%
Natus Medical Incorporated	Against	24.5%
Tabula Rasa HealthCare, Inc.	Against	24.6%
Montrose Environmental Group, Inc.	Against	25.1%
RLJ Lodging Trust	Against	26.2%
Netflix, Inc.	Against	26.9%
D.R. Horton, Inc.	Against	27.4%
Hepion Pharmaceuticals, Inc.	For	28.5%
TG Therapeutics, Inc.	Against	29.5%
Neogenomics, Inc.	Against	30.6%
JPMorgan Chase & Co.	Against	31.0%
Tutor Perini Corporation	Against	31.5%
Booking Holdings Inc.	Against	31.7%
Nabors Industries Ltd.	Against	32.2%
2U, Inc.	Against	33.4%

Griffon Corporation	Against	33.5%
Centene Corporation	Against	33.6%
Intel Corporation	For	33.9%
nLIGHT, Inc.	Against	34.5%
ServiceNow, Inc.	Against	35.0%
FLEETCOR Technologies, Inc.	Against	35.6%
CONSOL Energy Inc.	For	35.6%
AMC Entertainment Holdings, Inc.	Against	36.0%
Waitr Holdings Inc.	Against	36.6%
Barnes Group Inc.	Against	37.4%
Welbilt, Inc.	For	38.4%
Ring Energy, Inc.	For	38.9%
Heska Corporation	Against	39.4%
Castle Biosciences, Inc.	For	40.2%
Harley-Davidson, Inc.	Against	40.4%
Hexcel Corporation	Against	41.0%
Global Payments Inc.	Against	41.1%
Penn National Gaming, Inc.	Against	41.8%
Transmedics Group, Inc.,	Against	42.0%
UroGen Pharma Ltd.	Against	42.1%
Smartsheet Inc.	Against	42.8%
MEDNAX, Inc.	Against	43.2%
Sage Therapeutics, Inc.	For	43.4%
Natural Gas Services Group, Inc.	For	43.6%
Vector Group Ltd.	Against	43.9%
JBG SMITH Properties	Against	44.0%
Mersana Therapeutics, Inc.	Against	44.1%
Yellow Corporation	Against	44.6%
Advaxis, Inc.	For	44.9%
Cardiff Oncology, Inc.	Against	45.8%
Halliburton Company	Against	46.2%
Heritage-Crystal Clean, Inc.	Against	46.2%
Amarin Corporation plc	For	46.3%
Quotient Technology Inc.	For	46.3%
Health Catalyst, Inc.	Against	46.4%
Dime Community Bancshares, Inc.	For	46.5%
Zurn Water Solutions Corporation	Against	46.6%

Masimo Corporation	Against	47.0%
Enphase Energy, Inc.	For	47.4%
The RealReal, Inc	For	47.5%
IMAX Corporation	Against	47.7%
Talos Energy Inc.	Against	47.9%
SS&C Technologies Holdings, Inc.	For	48.0%
Servotronics, Inc.	For	48.2%
The TJX Companies, Inc.	For	48.2%
Wynn Resorts, Limited	Against	48.5%
Allegheny Technologies Incorporated	Against	48.7%
Ventas, Inc.	For	48.9%
Paycom Software, Inc.	Against	49.2%
Nicolet Bankshares, Inc.	Against	49.4%
Titan International, Inc.	Against	49.8%
Ultragenyx Pharmaceutical Inc.	For	50.0%

Failed Golden Parachute Proposals

Company	Glass Lewis Recommendation	Shareholder Support
Great Western Bancorp, Inc.	For	37.9%
Rogers Corporation	Against	18.2%
Umpqua Holdings Corporation	For	35.0%
SPX FLOW, Inc.	For	28.5%
CMC Materials, Inc.	For	35.6%
Bottomline Technologies, Inc.	For	49.2%
Citrix Systems, Inc.	For	36.6%
Quidel Corporation	For	36.2%
TEGNA Inc.	Against	29.5%
Tenneco Inc.	For	44.9%
Alleghany Corporation	Against	39.7%

GLASS LEWIS

Failed Equity & Non-Executive Compensation Proposals

Company	Glass Lewis Recommendation	Shareholder Support
Great Western Bancorp, Inc.	For	37.9%
Rogers Corporation	Against	18.2%
Umpqua Holdings Corporation	For	35.0%
SPX FLOW, Inc.	For	28.5%
CMC Materials, Inc.	For	35.6%
Bottomline Technologies, Inc.	For	49.2%
Citrix Systems, Inc.	For	36.6%
Quidel Corporation	For	36.2%
TEGNA Inc.	Against	29.5%
Tenneco Inc.	For	44.9%
Alleghany Corporation	Against	39.7%

GLASS LEWIS

Appendix D

Majority Supported Shareholder Proposals

Ticker	Company Name	Proposal Type	GL Rec	MGMT Rec	2022 Support	2021 Support	Proponent
				Compensation			
ABBV	AbbVie Inc.	Severance Policy	For	Against	50.4%		John Chevedden on behalf of Kenneth Steiner
ALK	Alaska Air Group, Inc.	Severance Policy	For	Against	54.5%		John Chevedden
FISV	Fiserv, Inc.	Severance Policy	For	Against	50.7%		Not disclosed
SPR	Spirit AeroSystems Holdings, Inc.	Severance Policy	For	Against	67.5%		John Chevedden
				Environmental			
BA	The Boeing Company	Climate Reporting	For	For	91.4%		Not disclosed
BLDR	Builders FirstSource, Inc.	GHG Reduction Targets	For	Undetermined	87.6%		Green Century Capital Management, Inc.
CAT	Caterpillar Inc.	GHG Reduction Targets	For	For	96.5%		As You Sow on behalf of Longview Large Cap 500 Index Fund and co-filer
CB	Chubb Limited	GHG Reduction Targets	For	Against	72.2%		As You Sow, as representative of the As You Sow Shareholder Action Account
COST	Costco Wholesale Corporation	GHG Reduction Targets	For	Against	69.9%		Green Century Capital Management, Inc.
CVX	Chevron Corporation	Methane Emissions Disclosure	For	For	98.0%		Not disclosed
D	Dominion Energy, Inc.	Stranded Asset Risk	For	Undetermined	80.1%		Not disclosed
DLTR	Dollar Tree, Inc.	GHG Reduction Targets	For	Against	54.8%		As you Sow Shareholder Action Account
HD	The Home Depot, Inc.	Deforestation	Against	Against	64.7%		Green Century Capital Management, Inc.
JACK	Jack in the Box Inc.	Packaging	For	Against	95.4%		Green Century Management, Inc.
PSX	Phillips 66	Report on Plastics	Against	Against	50.4%		As You Sow, on behalf of Handlery Hotels, Inc.

GLASS LEWIS

TRV	The Travelers Companies, Inc.	GHG Reduction Targets	For	Against	55.8%		As You Sow, on behalf of Booth Investments, LLC.
USFD	US Foods Holding Corp.	GHG Reduction Targets	For	Undetermined	88.5%		Green Century Capital Management, Inc.
XOM	Exxon Mobil Corporation	Climate Accounting	For	Against	51.0%	49.4%	Christian Brothers Investment Services
				Governance			
A	Agilent Technologies, Inc.	Special Meetings	For	Against	81.7%		Myra K. Young
ALRM	Alarm.com Holdings, Inc.	Proxy Access	For	Against	52.7%		James McRitchie through his designee, John Chevedden
ANSS	ANSYS, Inc.	Board Declassification	For	Against	89.9%		Not disclosed
BDX	Becton, Dickinson and Company	Special Meetings	For	Against	54.2%	45.8%	Kenneth Steiner
CCK	Crown Holdings, Inc.	Special Meetings	For	For	99.1%		John Chevedden
CDW	CDW Corporation	Written Consent	For	Against	78.9%		John Chevedden
CERN	Cerner Corporation	Special Meetings	For	Against	74.4%		John Chevedden
CG	The Carlyle Group Inc.	Declassification	For	For	99.9%		Kenneth Steiner
CNC	Centene Corporation	Special Meetings	For	Against	55.2%		John Chevedden
COP	ConocoPhillips	Special Meetings	For	Against	53.0%		Kenneth Steiner
FTNT	Fortinet, Inc.	Simple Majority Vote	For	Undetermined	72.5%		John Chevedden
FTV	Fortive Corporation	Simple Majority Vote	Against	Against	55.3%		John Chevedden
GILD	Gilead Sciences, Inc.	Special Meetings	For	Against	56.8%		John Chevedden
GPN	Global Payments Inc.	Special Meetings	For	Against	50.4%		John Chevedden
GT	The Goodyear Tire & Rubber Company	Simple Majority Vote	For	Against	79.2%		John Chevedden
HCC	Warrior Met Coal, Inc.	Majority Vote for Director Elections	For	Against	66.5%		SEIU Master Trust
IQV	IQVIA Holdings Inc.	Majority Vote for Director Elections	For	Against	58.6%		Myra K. Young

JACK	Jack in the Box Inc.	Other	For	Undetermined	69.0%		The Humane Society of the United States
NCNO	nCino, Inc.	Majority Vote for Director Elections	For	Undetermined	98.8%		James McRitchie and Myra K. Young
NFLX	Netflix, Inc.	Simple Majority Vote	Against	Against	58.4%	90.1%	John Chevedden
NOC	Northrop Grumman Corporation	Special Meetings	For	Against	50.4%		John Chevedden
NSTG	Nanostring Technologies, Inc.	Board Declassification	For	Undetermined	99.8%		James McRitchie
NVTA	Invitae Corporation	Board Declassification	For	Against	56.3%		James McRitchie
NYCB	New York Community Bancorp, Inc.	Board Declassification	For	Undetermined	93.1%		Kenneth Steiner
OGE	OGE Energy Corp.	Simple Majority Vote	Against	Against	59.3%	86.2%	John Chevedden
SO	The Southern Company	Simple Majority Vote	For	For	98.4%		John Chevedden
TFX	Teleflex Incorporated	Simple Majority Vote	For	Against	95.3%		Not disclosed
TGNA	TEGNA Inc.	Special Meetings	For	Against	56.0%		Not disclosed
TKR	The Timken Company	Simple Majority Vote	For	Against	79.9%		John Chevedden
TTI	TETRA Technologies, Inc.	Simple Majority Vote	For	Undetermined	92.6%		Kenneth Steiner
TWOU	2U, Inc.	Majority Vote for Director Elections	For	Undetermined	97.9%		John Chevedden, on behalf of James McRitchie
				Social			
AAPL	Apple Inc.	Concealment Clauses	For	Against	50.0%		Not disclosed
AAPL	Apple Inc.	Civil Rights Audit	For	Against	53.6%		Not disclosed
ATVI	Activision Blizzard, Inc.	Report on Sexual Harassment and Discrimination	For	Against	67.4%		New York State Common Retirement Fund
DG	Dollar General Corporation	Electioneering Spending	For	Against	57.0%		John Chevedden
DIS	The Walt Disney Company	Pay Equity	For	Against	59.6%		Anne Butterfield

GLASS LEWIS

GILD	Gilead Sciences, Inc.	Lobbying Activities and Values Alignment	Against	Against	50.2%		Maryknoll Sisters of St. Dominic, Inc.
HD	The Home Depot, Inc.	Racial Equity Audit	For	Against	62.8%		The Service Employees International Union Master Trust
IBM	International Business Machines Corporation	Concealment Clauses	For	Against	64.7%		Jay Stanley Weisfeld Trust
JNJ	Johnson & Johnson	Racial Equity Audit	For	Against	62.6%	33.9%	Mercy Investment Services (Sisters of Mercy of the Americas), c/o Lydia Kuykendal
LOW	Lowe's Companies, Inc.	Pay Equity	For	Against	58.0%		Arjuna Capital, on behalf of Eleanor and Richard Shorter
MCD	McDonald's Corporation	Civil Rights Audit	For	Against	55.8%		SOC Investment Group
MMS	MAXIMUS, Inc.	Racial Equity Audit	For	Against	64.2%		The Service Employees International Union Pension Plans Master Trust
MO	Altria Group, Inc.	Civil Rights Audit	For	Against	62.2%		The Sisters of St. Francis of Philadelphia and seven co-filers
NFLX	Netflix, Inc.	Lobbying Report	For	Against	60.4%		Boston Common Asset Management
RGR	Sturm, Ruger & Company, Inc.	Human Rights	For	Against	68.5%		CommonSpirit Health
RUN	Sunrun Inc.	Concealment Clauses	For	For	98.2%		Nia Impact Capital
SRCL	Stericycle, Inc.	Civil Rights Audit	For	Against	60.6%		The International Brotherhood of Teamsters General Fund
TRV	The Travelers Companies, Inc.	Lobbying Report	For	Against	52.7%		First Affirmative Financial Network, on behalf of Amy Benesch
TWTR	Twitter, Inc.	Concealment Clauses	For	Against	68.9%		Whistle Stop Capital on behalf of Handlery Hotels Inc.
TWTR	Twitter, Inc.	Electioneering Spending	For	Against	53.4%		The New York State Common Retirement Fund and the Administrative Head of the New York State and Local Retirement System
WM	Waste Management, Inc.	Civil Rights Audit	Against	Against	55.0%		International Brotherhood of Teamsters General Fun

GLASS LEWIS

Connect with Glass Lewis

Corporate Website | www.glasslewis.com

Email | info@glasslewis.com

Social | @glasslewis | Glass, Lewis & Co.

Global Locations

North America

United States
Headquarters
255 California Street
Suite 1100
San Francisco, CA 94111
+1 415 678 4110
+1 888 800 7001

New York, NY
+1 646 606 2345

2323 Grand Boulevard
Suite 1125
Kansas City, MO 64108
+1 816 945 4525

Europe

Ireland
15 Henry Street
Limerick V94 V9T4
+353 61 292 800

United Kingdom
80 Coleman Street
Suite 4.02
London EC2R 5BJ
+44 20 7653 8800

Germany
IVOX Glass Lewis
Kaiserallee 23a
76133 Karlsruhe
+49 721 35 49 622

Asia Pacific

Australia
CGI Glass Lewis
Suite 5.03, Level 5
255 George Street
Sydney NSW 2000
+61 2 9299 9266

Japan
Shinjuku Mitsui Building
11th floor
2-1-1, Nishi-Shinjuku,
Shinjuku-ku,
Tokyo 163-0411, Japan

GLASS LEWIS

DISCLAIMER

© 2022 Glass, Lewis & Co., and/or its affiliates. All Rights Reserved.

This report is intended to provide a general overview of some of the issues that were up for shareholder vote during this past proxy season. It is not intended to be exhaustive and does not address all issues that were up for shareholder vote.

Glass Lewis provides its clients with research, data, and analysis of proxy voting issues, and makes recommendations as to how institutional shareholders should vote their proxies, without commenting on the investment merits of the securities issued by the subject companies. Therefore, none of Glass Lewis' proxy vote recommendations should be construed as a recommendation to invest in, purchase, or sell any securities or other property. Moreover, Glass Lewis' proxy vote recommendations are solely statements of opinion, and not statements of fact, on matters that are, by their nature, judgmental. Glass Lewis research, analyses, and recommendations are made as of a certain point in time and may be revised based on additional information or for any other reason at any time.

The information contained in this report is based on publicly available information. While Glass Lewis exercises reasonable care to ensure that all information included in this report is accurate and is obtained from sources believed to be reliable, no representations or warranties express or implied, are made as to the accuracy or completeness of any information included herein. Such information may differ from public disclosures made by the subject company. In addition, third-party content attributed to another source, including, but not limited to, content provided by a vendor or partner with whom Glass Lewis has a business relationship, as well as any Report Feedback Statement, are the statements of those parties and shall not be attributed to Glass Lewis. Neither Glass Lewis nor any of its affiliates or third-party content providers shall be liable for any losses or damages arising from or in connection with the information contained herein or the use or inability to use any such information.

Glass Lewis expects its subscribers to possess sufficient experience and knowledge to make their own decisions entirely independent of any information contained in its reports. Subscribers are ultimately and solely responsible for making their own voting decisions. Glass Lewis' reports are intended to serve as a complementary source of information and analysis for subscribers in making their own voting decisions and therefore should not be relied on by subscribers as the sole determinant in making voting decisions. All information contained in this document is protected by law, including but not limited to, copyright law, and none of such information may be copied or otherwise reproduced, repackaged, further transmitted, transferred, disseminated, redistributed or resold, or stored for subsequent use for any such purpose, in whole or in part, in any form or manner or by any means whatsoever, by any person without Glass Lewis' express prior written consent. This document should be read and understood in the context of other information Glass Lewis makes available concerning, among other things, its research philosophy, approach, methodologies, sources of information, and conflict management, avoidance and disclosure policies and procedures, which information is incorporated herein by reference. Glass Lewis recommends all clients and any other consumer of this document carefully and periodically evaluate such information, which is available at: http://www.glasslewis.com.

BETTER MARKETS

ESG FACT SHEET

ESG Investing is Here to Stay

The expression that people "vote with their feet" has never been more true than in the case of investing with regard to environmental, social, and governance (ESG) factors. Although in the case of ESG investing, perhaps the expression should be that people vote with their money. By year-end 2022, investor assets in sustainable investments amounted to $8.4 trillion, or about 12.6% of all U.S. assets under management.[1] And between 2019 and 2022, the share of index funds with an ESG mandate nearly doubled, from 3% to 5%.[2] These statistics demonstrate that investor demand for ESG funds means ESG investing is here to stay.

What is ESG?

ESG investing is a form of sustainable investing that considers environmental, social, and governance factors to judge an investment's financial returns and its overall impact.[3] Each of the three terms in "ESG" encompasses a variety of important aspects of corporate planning and operations that investors want to know about before deciding whether to invest in a company.

Environmental criteria reflect how a company contributes to, or mitigates, degradation of the environment. The most prominent example is a company's approach to climate change caused by greenhouse gas emissions: How does a company contribute to climate change, and how is the company addressing those risks and the climate change problem more generally? Environmental criteria may also reflect a company's energy use, its handling of waste and other pollutants, and its position on deforestation and other issues of natural resource conservation.

Social criteria examine a wide range of issues about social relations. A significant aspect is how the company treats its employees and whether it provides them with fair compensation and benefits. These factors also reflect the composition of a company's workforce: Does it reflect racial and gender diversity, and, importantly, is that diversity reflected up and down the corporate ladder? The "social" aspect of ESG also concerns whether the company's vendors reflect its own stated values and where the company stands on human rights issues.

Governance criteria deal with how well a company is managed by its leadership and whether the company has sufficient controls in place to ensure management serves the interests of, and is accountable to, various company stakeholders. Important components include executive

---

1 Ryan Ermey, *What is ESG Investing: A beginner's guide to choosing a sustainable fund*, CNBC (May 1, 2023), https://www.cnbc.com/2023/05/01/beginners-guide-to-esg-investing.html.

2 National Bureau of Economic Research, *Investors' Willingness to Pay for ESF Funds*, https://www.nber.org/digest/20231/investors-willingness-pay-esg-funds.

3 Alana Benson, *ESG for Beginners: Environmental, Social, and Governance Investing*, Nerdwallet (Feb. 21, 2023), https://www.nerdwallet.com/article/investing/esg-investing.

compensation that produces the right incentives for management, adequate board oversight, and robust auditing and other controls. Governance criteria also evaluate how the company treats shareholders and whether it provides them with the full and fair right to participate in corporate governance by voting through the proxy process.

Because investors are increasingly using the ESG criteria to make investment decisions that align with their core values, they need access to information about the degree to which companies have incorporated the ESG considerations into their structures and operations. This information enables investors to tailor their investment decisions and allocate their capital in ways they think are most effective in advancing their personal values. More disclosure about how companies are actually incorporating the ESG factors into their businesses will also help make those factors a reality. That, in turn, means progress toward increasing the sustainability, fairness, and quality of life our society can maintain. In short, to the extent profit-seeking companies see value in taking steps to prevent the ongoing degradation of the environment, address racism and sexism, reduce income inequality, and prevent fraud and other corporate malfeasance, all at the insistence of profit-seeking investors, the results will be market-based solutions, or at least mitigants, of some of our societies' most vexing problems.

Since roughly 2006, when the acronym "ESG" was first coined, more and more investors have been basing their investment decisions at least in part according to the way that companies incorporate the ESG factors into their operations, risk assessments, and planning processes. Indeed, investor demand has driven the growth of ESG investing.

Investors Continue to Demand ESG Investments

As discussed above, sustainable investments amounted to $8.4 trillion, or about 12.6% of all U.S. assets under management, by the end of 2022. In other words, 1 in every 8 U.S. investor dollar is in a sustainable fund.[4] And investors are increasingly choosing ESG criteria. According to a study of more than 1,000 global investors, 89% had adopted ESG in 2022, up from 84% in 2021.[5] Deutsch Bank found that more than half of investors (53%) regarded climate change as the most important factor affecting their investment decisions in 2022, up from 47% in 2021. A PwC survey in 2022 found that ESG issues are now among investors' top five concerns.[6] And PwC also estimated that ESG-focused institutional investment will rise 84% to $33.9 trillion in 2026, making up 21.6% of assets under management.[7] Bloomberg has gone even further, estimating that overall ESG assets

---

4 Erney, supra note 1.

5 Coryanne Hicks, *ESG Investing Trends for 2023*, U.S News & World Reports (Jan. 10, 2023), https://money.usnews.com/investing/investing-101/articles/esg-investing-trends.

6 Katie Mehnert and Hillary Homes, *What Investors Should Expect for ESG in 2023*, Nasdaq (Dec. 8, 2022), https://www.nasdaq.com/articles/what-investors-should-expect-for-esg-in-2023.

7 Leah Malone and Emily B. Holland, *ESG: Trends to Watch in 2023*, Harvard Law School Forum on Corporate Governance (Mar. 4, 2023), https://corpgov.law.harvard.edu/2023/03/04/esg-trends-to-watch-in-2023/.

may reach $53 trillion by 2025, representing more than a third of the $140.5 trillion in projected total AUM.[8]

The flow of money into sustainable funds buttresses these estimates. Inflows into ESG funds remained positive in 2022 despite market turmoil, with net inflows for U.S. ESG funds at $3 billion.[9] And ESG funds accounted for 65% of all inflows into European ETFs in 2022, up from 51% in 2021.[10] Non-ESG funds, by contrast, suffered outflows throughout 2022.[11] Similarly, in the first quarter of 2023, ESG funds enjoyed a quarter of net inflows, beating non-ESG funds, which lost money. Net inflows hit $25.5 billion across ESG debt, equity, and multi-asset funds, the best quarter since early 2022.[12] Investors are also willing to pay a premium for ESG index funds. Fund investors were willing to pay up to 28 basis points, or 0.28 percent annually, more for ESG funds. This is triple the 9-basis point premium they paid in 2019.[13]

Issuers have responded to investor demand with a multitude of ESG investing options. The U.S. Sustainable Investment Forum identified 645 registered investment companies with $1.2 trillion sustainable investment assets under management in 2022, including 444 mutual funds and 177 ETFs. The U.S. SIF also identified 383 alternative investment vehicles in 2022, including private equity and venture capital funds, hedge funds, and real estate investment trusts or other property funds, managing $762 billion in assets under management that considered ESG criteria.[14] Finally, the roughly 4,000 signatories to the Principles for Responsible Investment (PRI), a financial industry initiative that helps firms integrate environmental, social, and governance criteria into their investment and ownership decisions, represented more than $120 trillion of assets at the end of 2021, up from just $10 trillion in 2007.[15]

Investors Are Not Demanding Investments with an Anti-ESG Focus

Investor demand for ESG investments stands in sharp contrast to the lack of demand for investments with an anti-ESG focus. Anti-ESG investments arose in response to criticism of sustainable investing. However, these funds do not appear to be catching on with investors.

---

8 *ESG assets may hit $53 trillion by 20925, a third of global AUM*, Bloomberg (Feb. 23, 2021), https://www.bloomberg.com/professional/blog/esg-assets-may-hit-53-trillion-by-2025-a-third-of-global-aum/.

9 Ted Godbout, *Skepticism Aside, Asset Managers Push Forward with ESG Development*, National Association of Plan Advisers (May 19, 2023), https://www.napa-net.org/news-info/daily-news/skepticism-aside-asset-managers-push-forward-esg-development.

10 Emma Boyde, *ESG accounts for 65% of all flows into European ETFs in 2022*, Financial Times (Jan. 13, 2023), https://www.ft.com/content/a3e9d87f-fa6f-4e5e-be6e-e95b42af2fec.

11 Valentijn van Nieuwenhuijzen, *How Sustainability is Transforming the Economy and Creating Opportunities for Investors*, Goldman Sachs (Apr. 20, 2023), https://www.gsam.com/content/gsam/us/en/institutions/market-insights/gsam-insights/perspectives/2023/how-sustainability-is-transforming-the-economy.html.

12 Tommy Wilkes and Patturaja Murugaboopathy, *Banking turmoil dampens shine of ESG funds at end of strong Q1*, Reuters (Apr. 6, 2023), https://www.reuters.com/business/sustainable-business/banking-turmoil-dampens-shine-esg-funds-end-strong-q1-2023-04-06/.

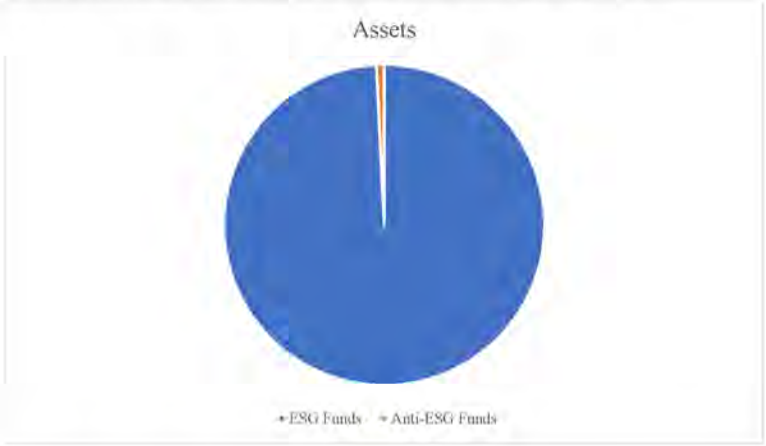
13 Rachel Layne, *As Climate Fears Mount, More Investors Turn to "ESG" Funds Despite Few Rules*, Harvard Business School (Mar. 23, 2023), https://hbswk.hbs.edu/item/as-climate-fears-mount-more-investors-turn-to-esg-funds-despite-few-rules.

14 U.S. Sustainable Investment Forum, *Sustainable Investing Basics*, https://www.ussif.org/sribasics.

15 *How Sustainability is Transforming the Economy and Creating Opportunities for Investors*, supra note 11.

Morningstar reports that sales of anti-ESG funds peaked at $377 million in the third quarter of 2022. Since that time, sales plunged to $188 million in the last quarter of 2022 and $183 million in the first quarter of 2023. The number of ESG funds also dwarfs that of anti-ESG funds. As noted above, there are hundreds of ESG investment vehicles. But Morningstar counted only 27 funds that it classified as anti-ESG. One anti-ESG fund launched in May 2022, picked up $870,000 on average in each quarter since, and filed for liquidation on June 2, 2023.

Overall, ESG funds outpace anti-ESG funds by nearly $270 billion to $2.1 billion.[16]



ESG Investments Offer Significant Financial Returns

A common refrain from those that oppose ESG investing and that promote anti-ESG funds is that sustainable investing means that financial results are forgone in order to achieve sustainable outcomes. But research shows that this assertion is not true. Rather, ESG and future profitability are linked. In other words, sustainable investing is not just about investing in companies that promote the best environmental, societal, and governance outcomes. Instead, looking at the investment universe through an ESG lens gives investors a comprehensive framework for how to identify companies that are best positioned for long-term profitability.

---

16 Joe Morris, *Anti-ESG Funds fail to gain traction in the US*, Financial Times (June 20, 2023), https://www.ft.com/content/e031fc3c-524b-4284-865f-e9849d424b02; Ross Kerber, *"Anti-ESG" funds face slowing deposits, Morningstar says*, Reuters (June 9, 2023), https://www.reuters.com/sustainability/anti-esg-funds-face-slowing-deposits-morningstar-says-2023-06-08/; David Hood and Yun Park, *Anti-ESG Funds Growing, Fail to Draw Major Investor Interest*, Bloomberg Law (June 9, 2023), https://news.bloomberglaw.com/esg/anti-esg-funds-slow-to-gain-major-investor-interest-report-says; Alyssa Stankiewicz and Mahi Roy, *The Anti-ESG Fad Might Be Over Before It Got Going*, Morningstar (June 7, 2023), https://www.morningstar.com/sustainable-investing/anti-esg-fad-might-be-over-before-it-got-going.

The reason for this advantage should be clear. The overwhelming scientific consensus is that climate change represents a potentially catastrophic threat and that the effort to combat climate change will lead to transformational change in all sectors of our society. In the face of these inevitable, pervasive, and powerful forces, it's easy to spot the smart investment: companies that are better prepared to deal with the impact of climate change and to compete in a decarbonized economy will likely be safer and better investments than companies that are not. So while many investors care about ESG issues because they want to advance policy goals, they also understand that companies that take the ESG factors seriously offer better financial returns.

To use environmental factors as an example, a company's strong environmental policies could have long-term benefits for their bottom line as it works towards thriving in a post-transition economy. Despite the assumption that companies that disregard environmental practices have lower overhead costs, research shows that ESG characteristics and profitability are linked. For example, companies that occupy LEED certified buildings tend to use less power, use renewable materials, and incorporate better construction methods in their buildings. Overall energy efficiency translates to lower operating costs. So occupying LEED certified buildings not only has a meaningful impact on building emissions but also leads to higher gross profitability and higher expected returns. The bottom line is that investors don't have to make performance concessions to achieve sustainable outcomes. ESG data is an indicator of future performance potential and should be incorporated into investors' decision-making. In other words, sustainability and financial profitability are inextricably linked.[17]

These sentiments come from the industry itself. Investment firms recognize that companies that transition successfully will be best positioned for success in the new sustainable economy. They argue that, for investors, this is not an impact bet but an understanding of where the economy is going. Investments that help accelerate the transition therefore have the potential to provide attractive financial returns.[18] For example, Goldman Sachs Global Investment Research found that stocks scoring higher for environmental and social criteria performed better than lower-scoring stocks for the first 11 months of 2022. This continued a trend stretching back more than a decade: in a study going back to the start of 2012, the lowest-ranking group of companies based on environmental and social criteria consistently underperformed the higher-ranking groups.[19] Indeed, since its establishment in 2019, the S&P Global 500 ESG Index has roughly tracked the standard S&P 500 Index, slightly outperforming it since 2020.[20]

Data from Morningstar has also found that sustainable investing generates returns similar to or better than those of the overall market. The broad Morningstar US Sustainability Index fell 18.9

---

17 Blackrock, *ESG X Big Data: Solving for the Double Bottom Line* (May 12, 2023), https://www.blackrock.com/us/individual/insights/decoding-the-markets-esg-x-big-data.

18 *How Sustainability is Transforming the Economy and Creating Opportunities for Investors*, supra note 11.

19 *Id.*

20 Karin Rives, *A "fiduciary question' looms large over the ESG debate in 2023*, S&P Global Market Intelligence (Jan. 26, 2023, https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/a-fiduciary-question-looms-large-over-the-esg-debate-in-2023-73830569.

percent in 2022, outperforming the 19.5% decline of its parent, the Morningstar US Large Mid-Cap Index. In the same period, the S&P 500 fell 19.4%.

Similarly, according to Morningstar's 2022 Sustainable Funds US Landscape Report, in 2021, most sustainable funds delivered stronger total and risk-adjusted returns than their respective Morningstar Category indexes. Slightly more than half of sustainable funds finished in the top half of their Morningstar category. Data for the previous five years showed even better results, as the returns of 74% ranked in the top half and 49% ranked in the top quartile returns.

In 2021, the Morgan Stanley Institute for Sustainable Investing found that in a year of extreme volatility, funds focused on environmental, social, and governance factors weathered the year better than non-ESG portfolios. The research analyzed more than 3,000 US mutual funds and ETFs, finding that sustainable equity funds outperformed non-ESG peers by a median total return of 4.3% in 2020. Meanwhile, sustainable taxable bond funds over the same period outperformed their peers by a median total return of 0.9%. In 2019, both sustainable equity funds and sustainable taxable bond funds also outperformed their traditional peer funds.[21]

Similarly, a 2019 white paper produced by the Morgan Stanley Institute for Sustainable Investing compared the performance of sustainable funds with traditional funds and found that, from 2014 to 2018, the total returns of sustainable mutual and exchange traded funds were similar to those of traditional funds. The study concluded that there is no financial trade-off in the returns of sustainable funds compared to traditional funds. The Morgan Stanley study also found that sustainable funds consistently showed a lower downside risk than traditional funds, regardless of asset class. The study found that during turbulent markets, such as in 2008, 2009, 2015, and 2018, traditional funds had significantly larger downside deviation than sustainable funds, meaning traditional funds had a higher potential for loss.

Finally, JUST Capital ranks companies based on factors such as whether they pay fair wages or take steps to protect the environment. It created the JUST U.S. Large Cap Diversified Index (JULCD), which includes the top 50% of companies in the Russell 1000 (a large-cap stock index) based on those rankings. Since its inception, the index has returned 15.94% on an annualized basis compared with the Russell 1000's 14.76% return.[22]

SEC Proposals

Investor demand for ESG investments coupled with the strong returns such investments offer means that investors need to know where companies stand on the ESG criteria and what investments incorporate ESG investing. One barrier to the continued growth of ESG investing is the lack of consistent reporting standards for ESG data.[23] Indeed, investors are increasingly demanding

---

21 *Sustainable Investing Basics*, supra note 14.

22 *Id.*; *ESG for Beginners*, supra note 3.

23 Brad Foster and David Tabit, *As demand for ESG investing grows, so too does the need for high-quality data*, Bloomberg (Apr. 22, 2019), https://www.bloomberg.com/professional/blog/demand-esg-investing-grows-need-high-quality-data/.

comprehensive, comparable, and reliable data related to ESG.[24] Fortunately, the SEC has proposed three rules that aim to provide investors with precisely that information.

First, the SEC has proposed a rule that would establish a mandatory disclosure regime for registrants in response to broad investor demand for better disclosure about how the companies they own are responding to the financial risks and opportunities presented by climate change. The rule would require that registrants disclose a variety of relevant data and information on their climate-related risks, metrics to assess climate-related risks, and strategies for addressing climate-related risks. If adopted, the rule would enhance the transparency of registrants' actions related to climate change, to the benefit of investors who are entitled to decision-useful information about how the companies they invest their money in are responding to one of the most urgent economic and financial risks our society faces.[25]

Second, the SEC has proposed a rule that would require investment companies, investment advisers, and other entities to disclose to investors information regarding their ESG investment strategies. The rule would establish a standardized ESG disclosure framework that would create more reliable, consistent, and comparable disclosures for ESG funds based on the extent to which a fund considers ESG factors in its investment selection and issuer engagement processes. If adopted, the rule would assist retail and institutional investors and satisfy growing investor demand for material information that can guide their investment decisions and protect them from misleading and abusive claims surrounding ESG investment strategies.[26]

Third, the SEC has proposed a rule that would ensure that the name of a registered investment company or business development company is not materially deceptive or misleading. The rule would strengthen the existing fund names rule and require that funds whose name suggests a focus on particular characteristics invest at least 80% of their assets in the type of investment suggested by their name. The rule uses the example of funds that indicate incorporation of one or more ESG factors in its investment selection process. The inclusion of terms such as "ESG" and "Sustainable" in fund names can lead to hundreds of millions of dollars of net flow to a fund. As a result, the rule would ensure that investors are not misled by a fund's name.[27]

---

24 *ESG: Trends to Watch in 2023*, supra note 7; James Killerlane, *How Issuers and Investors Can Find Common Ground on ESG*, Harvard Law School Forum on Corporate Governance (July 12, 2022). https://corpgov.law.harvard.edu/2022/07/12/how-issuers-and-investors-can-find-common-ground-on-esg/.

25 *See* The Enhancement and Standardization of Climate-Related Disclosures for Investors, 87 Fed. Reg. 21,334 (Apr. 11, 2022); Better Markets, Comment Letter on The Enhancement and Standardization of Climate-Related Disclosures for Investors (June 17, 2022). https://bettermarkets.org/wp-content/uploads/2022/06/Better_Markets_Comment_Letter_Enhancement_Standardization_Climate_Related_Disclosures.pdf.

26 *See* Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices, 87 Fed. Reg. 36,654 (June 17, 2022); Better Markets, Comment Letter on Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices (Aug. 16, 2022). https://bettermarkets.org/wp-content/uploads/2022/08/Better_Markets_Comment_Letter_ESG_Disclosures.pdf.

27 *See* Investment Company Names, 87 Fed. Reg. 36,594 (June 17, 2022); Better Markets, Comment Letter on Investment Company Names (Aug. 16, 2022). https://bettermarkets.org/wp-content/uploads/2022/08/Better_Markets_Comment_Letter_SEC_Investment_Company_Names.pdf.

The adoption of these three rule proposals would ensure that, along with their demand for ESG-related products, investors receive the information about the ESG factors that they need.

Conclusion

When it comes to ESG, the market has spoken. Investors want to invest in ESG investments, and businesses are satisfying that demand. Businesses and investors know that ESG is not simply about values; rather, it is about maximizing returns in a changing economy.

Indeed, the only thing that might prevent businesses and investors from realizing those returns is interference from legislators that normally favor free market solutions to societal problems.[28] Legislators have proposed a number of bills that aim to restrict fund managers' ability to consider ESG factors when making investments. Unsurprisingly, business leaders oppose these efforts. Recently, 270 businesses, banks, advocacy groups, and public retirement funds signed a "Freedom to Invest" initiative. The signatories urged federal and state lawmakers to protect their fiduciary duties and ability to make investment decisions that best serve their shareholders and beneficiaries for the long term. In addition to the California State Teachers Retirement System and the New York State Common Retirement Fund—two of the nation's largest pension programs—signatories included Boston Walden Trust Co., Trillium Investments LLC, and Franklin Templeton, as well as several other financial firms.[29]

The reason is that businesses recognize the importance of ESG. In 2022, Bloomberg conducted a study of global business leaders and found that the top motivation for considering ESG investing was the possibility of greater returns. And 71% of non-ESG fund managers said ESG was an important consideration when making investment decisions. Perhaps most significantly, 71% of all global business leaders said that, eventually, no investment decisions will be made without considering ESG.[30] It's fair to say that ESG investing is here to stay.

---

28 Maxine Joselow, *Some businesses say anti-ESG bills are anti-free market*, Wash. Post (June 22, 2023). https://www.washingtonpost.com/politics/2023/06/22/some-businesses-say-anti-esg-bills-are-anti-free-market/

29 Karin Rives, *270 companies, major pension funds join pro-ESG "Freedom to Invest" campaign*, S&P Global Market Intelligence (Mar. 20, 2023). https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/270-companies-major-pension-funds-join-pro-esg-freedom-to-invest-campaign-74862666.

30 Bloomberg, *The Future of ESG Investing*, https://sponsored.bloomberg.com/article/mubadala/the-future-of-esg-investing?srcf=mQvUqJZj.

BETTER MARKETS

Better Banks | Better Businesses

Better Jobs | Better Economic Growth

Better Lives | Better Communities

Better Markets is a public interest 501(c)(3) non-profit based in Washington, DC that advocates for greater transparency, accountability, and oversight in the domestic and global capital and commodity markets, to protect the American Dream of homes, jobs, savings, education, a secure retirement, and a rising standard of living.

Better Markets fights for the economic security, opportunity, and prosperity of the American people by working to enact financial reform, to prevent another financial crash and the diversion of trillions of taxpayer dollars to bailing out the financial system.

By being a counterweight to Wall Street's biggest financial firms through the policymaking and rulemaking process, Better Markets is supporting pragmatic rules and a strong banking and financial system that enables stability, growth, and broad-based prosperity. Better Markets also fights to refocus finance on the real economy, empower the buyside and protect investors and consumers.

For press inquiries, please contact us at press@bettermarkets.org or (202) 618-6430.

2000 Pennsylvania Avenue, NW | Suite 4008 | Washington, DC 20006 | 202-618-6464 | www.bettermarkets.org
© 2023 Better Markets, Inc. All Rights reserved.

July 11, 2023

The Honorable Patrick McHenry
Chairman
House Financial Services Committee
2134 Rayburn House Office Building
Washington, DC 20515

The Honorable Maxine Waters
Ranking Member
House Financial Services Committee
2221 Rayburn House Office Building
Washington, DC 20515

Dear Chairman McHenry, Ranking Member Waters, and Members of the Committee,

On behalf of Green America, I write in support of the Committee's important role in ensuring the efficiency, effectiveness, and accountability of the federal government and all its agencies.

Green America is the nation's leading green economy organization. Founded in 1982, Green America provides economic strategies, organizing power, and practical tools for businesses and individuals to solve today's social and environmental problems. We have over 300,000 individual members and supporters as well as almost 2,000 members in our Green Business Network. Our mission is to harness economic power — the strength of consumers, investors, businesses, and the marketplace — to create a socially just and environmentally sustainable society.

One of Green America's most important areas of work is responsible finance, including socially responsible investing, better banking, and shareholder advocacy. Our members and supporters are committed not just to talking about sustainability, but to aligning their money with their values, especially with regard to preserving a livable planet for current and future generations. Younger members in particular are interested in earning competitive returns with socially responsible investing.

We write to provide Green America's perspective regarding hearings on environmental, social, and corporate governance (ESG) convened by the House Financial Services Committee this July, including the preliminary report on ESG Climate Related Financial Services Concerns by the ESG Working Group.

We would like to challenge several underlying assumptions in this report and other memos from the majority, and clarify several important foundational truths:

- ESG performance is on par or better than conventional investing, especially in the long term.
- Environmental, social, and governance considerations are material and pecuniary, not political.
- The shareholder proxy voting process gives retail investors a critical voice in corporate governance, and reforms suggested by the majority would stifle, not promote, that voice.

ESG performance is on par or better than conventional investing, especially in the long-term.

Multiple research studies show that returns on socially responsible investing are on par or better than investing not based on ESG principles, especially over the long term. For example:

- According to Morningstar's 2022 Sustainable Funds US Landscape Report, most sustainable funds delivered stronger total and risk-adjusted returns than their respective Morningstar Category indexes. Over half of sustainable funds finished in the top half of their Morningstar Category, led by equity funds. Data for the previous five years showed even better results – the returns of 74 percent or sustainable funds ranked in the top half and 49 percent in the top quartile of returns.

- In 2021, the Morgan Stanley Institute for Sustainable Investing released a study, Sustainable Funds Outperform Peers during 2020 Coronavirus. The Institute found that in a year of extreme volatility and recession, funds focused on "on environmental, social and governance (ESG) factors, across both stocks and bonds, weathered the year better than non-ESG portfolios." The research analyzed more than 3,000 US mutual funds and ETFs, finding that sustainable equity funds outperformed non-ESG peer funds by a median of 4.3 percent in 2020.

- The NYU Stern Center for Sustainable Business released a 2021 meta study, ESG and Financial Performance: Uncovering the Relationship by Aggregating 1,000 Plus Studies Published between 2015-2020. The report found that 59 percent of studies showed that ESG investments had a similar or better performance relative to conventional investment approaches, while only 14 percent found negative results. It also concluded that "ESG investing appears to provide downside protection, especially during social or economic crises."

The reason ESG investing works is that it seeks out information about risk and opportunity that is not necessarily reflected on a company's balance sheet. For example, if a company routinely dumps toxic chemicals into communities where it works, underpays and overworks its employees, and skirts basic safety practices, that poses a financial risk. Eventually these poor practices will catch up with that company, and investors and shareholders will be caught holding the bag. On the flip side, if a company takes advantage of burgeoning markets in clean energy, provides fair pay and benefits for its workers, and contributes to its community, that company is positioned for stable growth and greater profitability.

ESG investing exists because millions of Americans, including Green America's members and supporters, want to invest in companies that practice it. That's why $8.4 trillion – or $1 in $8 under asset management – are invested in sustainable assets as of 2022, according to the US SIF Foundation's Report on US Sustainable Investing Trends. Socially responsible investing that takes environmental, social, and corporate governance (ESG) factors into account has been steadily growing for decades.

Using ESG principles to help inform investing is not a breach of fiduciary duty. On the contrary, **not** taking all factors related to risk and opportunity into account could be seen as a breach of fiduciary duty. Individual, institutional, and public asset managers should be free to consider all information when making critical investment decisions. This is how the free market works. It is not the role of government on the federal or state level to tell asset managers how to manage investments for their clients.

Environmental, social, and governance considerations are material and pecuniary, not political.

Environment

The economic risks and impacts of the climate crisis are real. This March, the Intergovernmental Panel on Climate Change – the world's climate scientists – issued a "final warning" to humanity that we must act immediately and decisively to lower greenhouse gas emissions in order to avoid runaway global warming that will irreversibly harm the one planet humans have ever called home. We are already experiencing the economic impacts of climate events, from storms to droughts to extreme heat and cold.

Companies face physical risks resulting from climatic events, such as wildfires, storms, and floods. According to the National Oceanic and Atmospheric Administration, the year 2022 saw 18 billion-dollar-or-more weather and climate disasters that caused $176.9 billion in damages, the third-highest year on record. The number of such events has been steadily rising, with 33 in all of the 1980s, 57 in the 1990s, 67 in the 2000s, 131 in the 2010s, and we are already 60 just three years into the 2020s with 1,460 deaths and counting. Already 2023 is shaping up to be the hottest year on record, with the hottest day ever recorded in human history on July 4. Extreme heat is now killing more Americans than ever.

So far the earth has warmed 1.2°C since pre-industrial times. Deloitte finds that if we allow warming to reach 3°C, the global economy will lose $178 trillion by 2070 through a lack of food and water, a loss of jobs, worsening health and well-being, and reduced standard of living. On the flip side, if the world acts now to achieve net zero emissions by 2050, the transformation of the economy could increase the size of the world economy by $43 trillion in net present value terms from 2021-2070.

Companies also face both risk and opportunity from policy action needed to transition the economy off fossil fuels. Companies that invest in clean energy and energy efficiency are booming. Global renewable power capacity is now expected to grow by 2,400 gigawatts over the next five years, an amount equal to the entire power capacity of China today, according to the International Energy Agency. Despite uncertainty in the overall economy, jobs in the clean energy industry have seen double-digit increases, especially in Michigan, Texas, California, and West Virginia, according to the Department of Energy.

On the flip side, fossil energy of the past must be phased out – and the fossil fuel industry knows it. Last year the fossil fuel industry made record profits – but instead of using that money to transition their business model to the clean energy of the future, they are doubling down on fossil-fuel extraction – and bankrolling efforts to prevent workers from using their retirement investments to push companies to address the social and environmental concerns that negatively affect them and our financial system.

At its heart, this fight is about how large corporations should behave in our society: Should they focus on short-term, risky value extraction or long-term, sustainable value creation? Retirement funds, pensions, endowments, and college funds rely on long-term investments, where ESG makes a material difference.

Social
Failure to address racial equity issues within a company creates risks for shareholders, including risk of reputational damage, litigation, and adverse policy and regulatory action. Company actions that contradict stated positions create substantial risks and raise concerns about the adequacy of governance and oversight. Such actions entail significant costs to both the company and the economy.

Failure to address racial gaps for Black Americans in wages, housing, education, and investment has cost the U.S. economy $16 trillion over the last 20 years, according to a Citi analysis of the economic cost of racial inequality in the United States. If those gaps were closed, $5 trillion could be added to U.S. GDP over 5 years -- a primary driver of returns for long-term investors.

That is why shareholder proposals related to racial equity received strong support in 2022. A majority of the 20 largest asset managers — those with more than $1 trillion in assets under management — voted in favor of a majority of shareholder proposals on racial equity audits, board diversity, political spending and lobbying activity, human capital management, and tech company product and service issues, according to the Equity in the Boardroom report from February 2023.

Racial equity audits — an essential mechanism for management and oversight of risks associated with systemic racism — saw increased support from shareholders in 2022, with average support increasing from 33 percent to 44 percent, and six receiving majority support, the report said.

Governance

A company's political spending and lobbying can present significant reputational risk if not disclosed and managed. Many customers and the purchasing public – including Green America's members and supporters -- are paying close attention to whether a company's lobbying lines up with its corporate values. If there is a disconnect, companies face bad press, boycotts, or targeted social media campaigns.

According to the Conference Board, 87 percent of companies say the environment for corporate political activity is the most challenging in memory and likely to become even more so. Corporate political activity is being scrutinized not just by the media and employees, but by shareholders who are focused on whether a company's lobbying and political contributions are consistent with its public stances.

Customers and shareholders are concerned about corporate political spending and lobbying because a functioning democracy is foundational to a stable economy and sustainable long-term value creation. The United States is experiencing an erosion of democracy, as evidenced by decreased public trust in elections, voter suppression efforts, lack of transparency regarding political spending and lobbying, among other concerning trends, according to the Brookings Institution.

Costs of anti-ESG legislation

This year 165 anti-ESG bills and resolutions were introduced in 37 states. Some legislation requires state treasurers or comptrollers to create a blacklist of companies the state is not allowed to invest in or do business with. Such restrictions result in significant costs:

- A Wharton School study found that two 2021 Texas laws banning cities from contracting with banks that have ESG policies cost an extra $303 million to $532 million in higher municipal bond interest rates.
- A report by Econsult Solutions found that taxpayers in Florida, Kentucky, Louisiana, Missouri, Oklahoma, and West Virgina could owe up to $708 million in additional interest charges on municipal bonds due to anti-ESG laws and proposals.
- A Bloomberg article shows that Texas is paying 19 basis points more than California and Florida is paying 43 basis points – almost half a percentage point – more in interest rates on the bond market because they prohibit contracts with lenders that consider ESG.
- Indiana's budget office found that a bill forcing pension funds to divest from asset managers that consider ESG factors would cost $6.7 billion over the next decade in sub-market returns, force retirees to increase their contributions, and impose an additional $550,000 in administrative costs per year. Amended legislation now puts the estimated costs to pensions funds at $5.5 million.
- The Kansas Division of the Budget found that an anti-ESG bill could cost the Kansas Public Employees Retirement System upwards of $3.6 billion over the next ten years.

Public support for ESG

Despite the concerted campaign to push anti-ESG bills across dozens of states, multiple polls and focus groups show that public opinion clearly supports responsible investing.

- A poll by Penn State and ROKK Solutions found that 63% of respondents – including 70% of Republicans -- say the government should not set limits on ESG investments. The poll found 76% of voters feel companies play a vital role in society and should be held accountable to make a positive impact on the communities in which they operate. This finding is consistent across political lines, with a majority of both Republicans (69%) and Democrats (82%) in agreement.
- In focus groups conducted by JUST Capital in December 2022, participants said companies should be "good corporate citizens" and make a positive impact on society, especially by paying their employees a fair, living wage. They also saw ESG as part of a sound investment strategy.
- Polling by Climate Power and Data for Progress in March 2023 found that most respondents think financial managers should be able to consider ESG factors in investment decisions, and they support investing public retirement funds in clean energy assets.

Investors also see ESG as a critical part of their fiduciary duty: 85% of investors are interested in responsible investing, 86% believe companies with sustainability practices may be better long-term investments, and 84% are interested in sustainable investments that can be tailored to their needs, according to US SIF: The Forum for Sustainable and Responsible Investment.

The shareholder proxy voting process gives retail investors a critical voice in corporate governance, and reforms suggested by the majority would stifle, not promote, that voice.

The ESG Working Group's preliminary report on ESG Climate Related Financial Services Concerns lists as its top priority "reform of the proxy voting system to safeguard the interests of retail investors." However, the revisions this report calls for would squash a critical tool that allows retail investors to protect their investments by providing an efficient way to communicate their views on material issues.

The SEC shareholder proposal rule, in place for 50 years, has been used to encourage companies to adopt policies that are now widely viewed as best practice, driven initially by shareholder proposals. For example, electing directors by majority vote rather than a plurality was a radical idea when shareholders first proposed it over a decade ago, but is now the norm at large-cap U.S. companies. SEC rules exclude proposals that address the day-to-day management of companies but preserve the right of investors to debate perspectives on emerging issues that are relevant to companies' futures.

We would like to address some specific claims made by the ESG Working Group's preliminary report.

Shareholder proposals are not a significant burden for public companies.
The only mandatory cost under the shareholder proposal rule is for the company to publish a proposal of up to 500 words on its proxy ballot. All other spending is discretionary, and almost all shareholder proposals are non-binding. The board does not have to do anything in response to a proposal.

Shareholder proposals constitute a small percentage of overall proxy votes each year. According to the Council of Institutional Investors, most public companies do not receive any shareholder proposals. On average, 13% of Russell 3000 companies received a shareholder proposal in a particular year between 2004 and 2017. In other words, the average Russell 3000 company receives a shareholder proposal once every 7.7 years. For companies that receive a shareholder proposal, the median number is one per year.

Raising thresholds for ownership and resubmission would squash the voice of small investors.
Currently, in order to file a shareholder resolution at a given company, a person must have owned at least $2,000 of company securities for at least one year. The working group proposes raising that

threshold to continuous ownership of at least $2,000 of the company's securities for at least three years; continuous ownership of at least $15,000 of the company's securities for at least two years; or continuous ownership of at least $25,000 of the company's securities for at least one year.

Such revisions would hamper the participation of small and diverse investors in the shareholder resolution process. These smaller investors can have a great impact on corporate practice. According to data compiled by the Sustainable Investments Institute, 176 resolutions on social and environmental topics came to a vote at U.S. companies in 2019. Many were filed by investors with small ownership thresholds. The proposals received an average of 25.5% support, demonstrating that proposals of interest to a large portion of a company's shareholder base can originate with smaller investors.

Likewise, the working group proposes raising the voting thresholds needed to resubmit a shareholder resolution from 3%, 6% and 10% in the first, second and third year respectively, to a vote of 5%, 15%, and 25% in order to resubmit a shareholder resolution the following year. Again this would squash the voice of small and diverse investors, especially as concerns emerging issues.

In some cases, it can take years for issues such as climate risks, human rights assessments, and governance reforms to be recognized as important to a company's returns. Through long-term investor engagement and education, corporate boards and shareholders often eventually do adopt proposals that had less support at first but are now seen as best practices.

In 2020, the SEC raised ownership and resubmission thresholds to respond to pressure from corporate trade associations, presenting significant hurdles to filing and resubmitting shareholder proposals. Raising these thresholds again would shut out small investors and leave emerging issues unaddressed.

Proxy advisory firms do not wield excessive influence over investors.
Many pension funds and other institutional investors review research and recommendations from proxy advisors but vote according to their own guidelines and policies. According to proxy advisor ISS, 85% of its top 100 clients use a custom voting policy.

Institutional investors do not "robo vote" proxy advisor recommendations. An NYU-UPenn study finds that the impact of recommendations by ISS is significantly reduced when company-specific factors are taken into account. The proposed curbs on proxy advisors could undermine the voice of investors by limiting the information available and further tilting votes on key proposals in favor of management.

Thank you for your consideration of these important matters regarding responsible finance. Please do not hesitate to reach out if you have any questions or would like any other information.

Sincerely,

Cathy Cowan Becker
Responsible Finance Campaign Director
Green America

cc: Members of the House Financial Services Committee
cc: Members of the House Sustainable Investment Caucus

INTERFAITH CENTER ON CORPORATE RESPONSIBILITY
Inspired by faith. Committed to action

July 5, 2023

The Honorable Patrick McHenry
Chairman
Financial Services Committee
U.S. House of Representatives

The Honorable Maxine Waters
Ranking Member
Financial Services Committee
U.S. House of Representatives

Dear Chairman McHenry and Ranking Member Waters,

As a coalition of faith and values-based institutional investors with over 50 years of experience in ESG investing, we are writing to contribute our perspective for the record regarding the hearings on ESG convened by the House Financial Services Committee this July. Members of the Interfaith Center on Corporate Responsibility (ICCR) are active and diversified portfolio owners raising material concerns with companies that affect shareholder value and create broader systemic risks.

Religious investors were early pioneers in this field going back to the early 1970s and representatives of faith-based pension funds and endowments can testify to their experience as thoughtful fiduciaries committed to creating financial value for their clients and beneficiaries while advocating from the inside for corporate changes in policies and practice to address critical social and environmental challenges. As practitioners, we are glad to provide resources to assist members of the committee in refuting any arguments presented during the hearing attempting to discredit ESG investing as a sound and safe risk-mitigation strategy.

We include a letter we circulated to Members of Congress earlier this month, which responds to a number of the arguments against ESG investing and further describes our long-term experience as fiduciaries actively employing ESG strategies.

Please reach out to us if we can be of any assistance.

Sincerely,

Josh Zinner
Chief Executive Officer
Interfaith Center on Corporate Responsibility

475 Riverside Drive, Suite 1842, New York, NY 10115 (212) 870-2295
www.iccr.org

Out Leadership
135 W 26th Street, Suite 7A
New York, NY 10001
(212)507-9660
outleadership.com

June 20, 2023

The Honorable Patrick McHenry (R-NC)
Chairman
U.S. House Committee on Financial Services
Washington, D.C. 20515

The Honorable Glenn Thompson (R-PA)
Chairman
U.S. House Committee on Agriculture
Washington, D.C. 20515

The Honorable Maxine Waters (D-CA)
Ranking Member
U.S. House Committee on Financial Services
Washington, D.C. 20515

The Honorable David Scott (D-GA)
Ranking Member
U.S. House Committee on Agriculture
Washington, D.C. 20515

Re: An Open Letter from Out Leadership on the Business Case for ESG Reporting & Investment.

Dear Chairman McHenry and Thompson and Ranking Members Waters and Scott:

Out Leadership is writing to you today in support of the continuation and expansion of Environmental, Social, and Governance (ESG) reporting and metrics, and to oppose the contraction or eradication of ESG policies. ESG policies, procedures, reporting, and implementation have delivered positive business outcomes, which have led to the adoption of these efforts by thousands of companies, including a supermajority of US-based Fortune 500 companies, over the last two decades. Businesses will only do what is in their bottom line, sustainable best interest to deliver shareholder value. The simple fact that companies themselves have sought to implement ESG initiatives, without regulation by Congress, is proof. Congressional limitations on ESG efforts will severely hamper companies' abilities to do better business and meet investor demand.

As the premier global LGBTQ+ business advocacy platform, which counts 88 of the world's most powerful companies as members (see Appendix I), Out Leadership understands the needs of our companies and has seen the results of ESG efforts (for more information about Out Leadership, see Appendix II).

OUTLEADERSHIP

Out Leadership has been the undisputed global voice of the business community on issues of LGBTQ+ equality since 2010. Fundamental to our mission is achieving the integration of measurable LGBTQ+ representative data for Diversity, Equity, and Inclusion (DEI) into the growing global use of ESG practice and reporting.

Despite current conversation, ESG is not a new concept. Companies have been evaluating ways to maximize returns, mitigate risks, and create business opportunities by analyzing ESG-related issues for decades. Increasingly, they recognize that understanding and reporting to shareholders on their human capital is core to a healthy bottom line, and that a workforce that is diverse, in every sense of the word, leads to better decision-making that is key to long-term success.

ESG is integral to improving consumer, employee, and investor satisfaction and, ultimately, company performance. Our research bears this out. Factors include: (1) investor demand, (2) measurable risk management, and (3) corporate culture that recruits and retains top-tier talent.

These activities are not political pandering fads – they drive results. Asking, or in the case of some Congressional leaders, demanding that companies cease diversity and inclusion activities, and now ESG efforts, are forcing companies to act contrary to their financial interests and the desires of their investors. **A company's primary responsibility is to its shareholders, and Congress should not obstruct, but rather create opportunities in the market.**

Here is the key research that supports our position:

1. Investors are increasingly demanding sustainability.

- **The demand is clear.** According to the Global Sustainable Investment Alliance (GSIA), as of 2020, sustainable investment assets globally reached $35.3 trillion, representing a 15% increase from 2018.[1] This indicates a significant and growing interest among investors in further incorporating ESG factors into their investment strategies.
- **There is a strong positive correlation between ESG performance and financial performance.** A study by Friede, Busch, and Bassen analyzed over 2,000 empirical studies and found a positive relationship between ESG factors and corporate financial performance in the majority of cases.[2]
- Research from Out Leadership and BRANDthrō surveying US CEOs and employees found that a distinctive **majority of both CEOs and employees recognize that ESG is important to their business.**[3]

[1] "Global Sustainable Investment Review 2020," The Global Sustainable Investment Alliance (GSIA), 2021, https://www.gsi-alliance.org/.
[2] Friede, G., Busch, T., & Bassen, A. (2015). "ESG and financial performance: Aggregated evidence from more than 2000 empirical studies," *Journal of Sustainable Finance & Investment*, 5(4), 210–233. https://doi.org/10.1080/20430795.2015.1118917
[3] Preliminary analysis conducted by Out Leadership, PwC, and BRANDthrō (2023).

2. ESG mitigates business risks.

- **ESG considerations help investors assess and manage various risks associated with environmental, social, and governance issues.** For instance, companies with poor environmental practices may face lawsuits, regulatory penalties, reputational damage, or increased costs. Evaluating these factors helps investors identify potential risks and avoid investments that could be negatively impacted.
- **When boards are diverse, they perform.** Diverse boards make better decisions and lead to greater returns on investment for businesses. A Harvard study found that when Fortune 500 companies were ranked by the number of women on their boards, those in the highest quartile reported a 42% greater return on sales and a 53% higher return on equity.[4] Companies know that diversity is good for business and are following suit – across the Fortune 500, the number of companies with LGBTQ+-inclusive board diversity policies has risen from just 2 companies in 2015 to 112 companies in 2023.[5]
- ESG-focused investments have demonstrated resilience during market downturns. A study by Arabesque and the University of Oxford analyzed 200 academic papers and found that **88% of them reported a positive correlation between ESG factors and resilience to systemic shocks**.[6]
- **Increasingly, customers look at a company's performance on DEI when making their purchasing decisions.** A study by Bain & Company of 4,000 US consumers published in June 2023 found that 30% of Generation Z would reject a brand because of the company's inability to share its DEI track record.[7]

3. Modern businesses and employees of the future demand ESG and LGBTQ+-inclusive diversity.

- According to a survey by Deloitte of 5,474 LGBTQ+ people across 13 countries published in June 2023, a third of respondents are actively **looking to change employers to find an organization that is more LGBTQ+ inclusive**.[8] That same survey reveals that more than half of respondents cite a company's external commitment to LGBTQ+ inclusion as a deciding factor on whether to apply. And one in two of Gen Z office workers look at sustainability reports when researching a job according to a study published by KPMG in January 2023.[9]

---

[4] "Why Diversity Matters: Women on Boards of Directors." Executive and Continuing Professional Education, July 21, 2016. https://www.hsph.harvard.edu/ecpe/why-diversity-matters-women-on-boards-of-directors/.
[5] "LGBTQ+ Board Diversity: Progress & Possibility," Out Leadership, April 19, 2023, https://outleadership.com/driving-equality/board-diversity-2023-progress-possibility/.
[6] "From the stockholder to the stakeholder," Arabesque, 2020, https://www.arabesque.com/2020/02/04/from-the-stockholder-to-the-stakeholder/.
[7] "Does a purpose help brands grow?," Bain, June 5, 2023. https://www.bain.com/insights/does-a-purpose-help-brands-grow/.
[8] "The Deloitte Global 2023 LGBT+ Inclusion @ Work Survey reveals a third of respondents are looking to change jobs as they want a more LGBT+ inclusive employer," (2023, June 22). Deloitte. https://www.deloitte.com/global/en/about/press-room/deloitte-global-2023-lgbt-inclusion-work-survey.html
[9] "Climate quitting—Younger workers voting with their feet on employer's ESG commitments—KPMG United Kingdom." KPMG, January 24, 2023, https://kpmg.com/uk/en/home/media/press-releases/2023/01/climate-quitting-younger-workers-voting-esg.html.

- As many as 20% of Gen Z identifies as LGBTQ+.[10] The LGBTQ+ population is on track to be similar in size to the Black and Hispanic populations, which currently account for 13.6% and 19.1% of Americans, respectively.[11] **Companies risk alienating what is set to be one-fifth of their talent pool** (as well as a much larger group consisting of allies – which represent the vast majority of Americans according to the latest Gallup poll on LGBTQ+ rights[12]) if they fail to communicate a compelling narrative on how they support LGBTQ+ workers and the LGBTQ+ community more broadly.
- **Top companies understand the importance of inclusive business for attracting and retaining talent.** Out Leadership found that across the Fortune 100:
    - 35% of companies share the results of their LGBTQ+ Workplace Equality Indices and demonstrate the global breath of their LGBTQ+ DEI efforts.
    - 45% of companies include LGBTQ+-owned businesses within the scope of their supplier diversity program.
    - 50% of companies have joined the Human Rights Campaign (HRC) Business Coalition for the Equality Act.[13]

Out Leadership and our member companies stand ready to continue to support Congress in protecting companies ability to do the best business on behalf of all their shareholders.

Sincerely,

Todd G. Sears
Founder & CEO
Out Leadership

[10] "LGBT Identification in U.S. Ticks up to 7.1%." 2022, Gallup, February 17, 2002, https://news.gallup.com/poll/389792/lgbt-identification-ticks-up.aspx.
[11] "U. S. Census bureau quickfacts: United states." (n.d.). Retrieved July 10, 2023, from https://www.census.gov/quickfacts/fact/table/US/RHI225222.
[12] "U.S. Same-Sex Marriage Support Holds at 71% High." Gallup , June 5, 2023, https://news.gallup.com/poll/506636/sex-marriage-support-holds-high.aspx.
[13] Preliminary analysis conducted by Out Leadership (2023).

OUTLEADERSHIP

Appendix I

1. Alix Partners
2. Amazon
3. American Express
4. American Securities
5. Apollo Global Management
6. Bain Capital
7. Baker Donelson
8. Baker Hostetler
9. Bank of America
10. Barclays
11. Brown Brothers Harriman
12. BIO – Biotechnology Innovation Organization
13. BlackRock
14. Blackstone
15. Bloomberg LP
16. BMI
17. CalPERS
18. Citigroup
19. Coca-Cola
20. Comcast
21. Corrs, Chambers, & Westgarth
22. Covington & Burling
23. Cowen Inc.
24. Cushman & Wakefield
25. DE Shaw
26. Diligent
27. DLA Piper
28. Dow Chemical
29. Edison International
30. Egon Zehnder
31. EY
32. FCB
33. Federal Reserve Bank of New York
34. FTI Consulting
35. First Republic Bank
36. Freshfields, Bruckhaus, Deringer
37. Genesis Trading
38. GLG
39. Gibson Dunn
40. Goldman Sachs
41. Greenberg Traurig
42. Henkel
43. Hogan Lovells
44. Hogarth
45. Hewlett Packard Ent.
46. HSBC
47. HSBC Life
48. I Heart Media
49. IBM
50. Jenner & Block
51. Johnson & Johnson
52. KKR
53. KPMG
54. LinkedIn
55. Littler
56. LVMH
57. Macquarie Group
58. Mastercard
59. McCann Worldgroup
60. Merryck & Co.
61.
62. Microsoft
63. Millennium Mgmt LLC
64. Mizuho
65. Moody's
66. Morrison & Foerster
67. MSCI Inc.
68. National Australia Bank
69. Nomura
70. Paul Weiss
71. Perpetual
72. PPG Industries
73. Publicis Sapient
74. PwC
75. RBC Capital Markets
76. Reed Smith
77. Ropes & Gray
78. Selendy & Gay
79. Shearman & Sterling
80. Simpson Thacher & Bartlett
81. Sullivan & Cromwell
82. T.Rowe Price
83. Twilio
84. Unilever
85. Visa
86. Wachtell, Lipton, Rosen, & Katz
87. Walmart
88. Wells Fargo
89. Zoomforth

Appendix II

Founded and based in New York City, Out Leadership is a tax-paying B Corporation, which also donates 20% of its pre-tax profits to LGBTQ+ charities. We work closely with our member companies and other partners to develop extraordinary talent, produce groundbreaking research, advance powerful advocacy, and improve business outcomes through CEO-hosted global summits and talent development initiatives in New York City, London, Hong Kong, and Sydney.

Out Leadership's 88 member companies (Appendix I) joined our coalition because they know that LGBTQ+ inclusion drives business returns across a wide spectrum of outcomes from talent attraction and development, to increased engagement, to direct business development. For 13 years, we have convened more than 112 CEO-hosted summits in five continents, engaging more than 30,000 senior executives, including 1,200+ CEOs. We have published 17 pieces of original research, most recently the Out Leadership LGBTQ+ Business Climate Index, which quantifies and tracks the impact of LGBTQ+ inclusion and discrimination across the fifty United States.

PRI Principles for Responsible Investment

July 12, 2023

Chair Patrick McHenry
Ranking Member Maxine Waters
Members of the Committee
U.S. House Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

Dear Chair McHenry, Ranking Member Waters and Members of the Committee,

The Principles for Responsible Investment (PRI) welcomes the opportunity to submit this statement for the record for the Committee on Financial Services hearing entitled, "Protecting Investor Interests: Examining Environmental and Social Policy in Financial Regulation."

The PRI is the world's leading initiative on responsible investment. We work to support investors in discharging their fiduciary duty by furthering the development of best practice on responsible investment, and helping our signatories understand how they can incorporate these practices to achieve their investment goals. Launched in 2006, the PRI now has more than 5,300 signatories globally (including asset owners such as pension funds and insurers, investment managers, and service providers) representing approximately $121 trillion in assets under management.[1] The PRI has more than 1,000 signatories based in the US.[2]

The Committee's attention on responsible investment issues is welcome and timely, as investors continue their efforts to adapt to an increasingly complex and quickly changing world. The industry is evolving its practices to account for the investment considerations affected by environmental, social and governance factors. These factors can significantly influence the financial risks and returns of their investment portfolios. As such, it is increasingly important to ensure investors have access to decision-useful information on related business activities that is consistent, comparable and standardized. This includes tools for consideration of all material data points to make informed investment decisions, reduce portfolio risk and meet the goals of their clients and beneficiaries. Investors also require the ability to express their rights as shareholders by carrying out robust stewardship programs—including via the proxy voting process—to fulfil their fiduciary duties to maximize returns.

Twice previously, in July 2019 and February 2021, the Committee held similar hearings and the PRI provided our perspective on the importance of supporting investors in their responsible investment practices.[3] In each of these prior letters, we highlighted the financial materiality of ESG factors, the necessity of consistent, comparable disclosure from issuers and the clarity needed for investors.

---

[1] As of July 6, 2023.
[2] An overview of the PRI's signatories is available on the PRI website: https://www.unpri.org/signatories/signatory-resources/signatory-directory.
[3] PRI, Letters to the Subcommittee on Investor Protection, Entrepreneurship and Capital Markets (February 25, 2021), available at: https://dwlyzx9upl8e.cloudfront.net/Uploads/h/i/l/pri_statement_for_the_record_hfsc_hearing_2_25_487428.pdf; and (July 10, 2019), available at: https://d8d913e8vf2o.cloudfront.net/Uploads/p/p/l/principlesforresponsibleinvestmentfinal_785719.pdf.

UN Global Compact | United Nations Global Compact

Responsible Investment Supports Fiduciary Duties

Responsible investment—including ESG integration—is not a new practice but has grown steadily in use and recognition over the past 50 years.[4] These topics have garnered increased attention as the materiality of ESG factors and relevance of responsible investment practices have become clearer, especially following the global COVID-19 pandemic. Responsible investment is a necessary evolution which enhances traditional financial analysis and portfolio construction techniques by considering financial risks and opportunities that may not be appropriately priced by the market. This involves broadening the perspective of an investor's decision-making to better account for all potentially relevant information that could impact the risk-return profile of investment decisions.

Responsible investment in no way forces investors to include or exclude specific investments, overweight specific considerations, or stray from their duties to clients and beneficiaries. There is no one way to be a responsible investor. Investors can use ESG information in many different ways throughout their investment and stewardship decisions. Incorporating material ESG information aids investors in making sure they are not ignoring or underweighting financially material issues when assessing risk and return. Depending on investment objectives, investors may apply an ESG-related process to their entire portfolio, on particular asset classes or on certain products. Different investors employ various strategies, leaving the choice of strategy up to the asset owner's (client's) decision.

Responsible investment practices support fiduciary duty by working to improve governance, disclosure and transparency across financial markets. As part of their responsibilities, fiduciaries consider risks, trends, opportunities and time-horizon (both short-term and long-term) when making investment decisions. The duties of prudence and loyalty are the inviolable core of every investor's responsibility. By advocating for stronger governance and transparency across financial markets, responsible investment supports participants at every level of the financial system to better assess actions both up and down the investment chain.

Environmental, Social and Governance Factors Are Material

ESG encompasses a broad range of overlapping factors that can influence the financial risk and return characteristics of an investment. ESG factors cover many different aspects, from climate change and resource scarcity (E) to working conditions and human rights violations (S) to bribery/corruption and executive compensation (G). These factors are used in investment analysis as better data show their increasingly material nature.[5] Growing attention to ESG reflects investors working diligently to ensure material risks and opportunities are appropriately assessed in order to protect and deliver for clients.

ESG integration is not an investment strategy, per se, but rather a process for formally considering a range of potentially material factors, for a more comprehensive understanding of financial risk and return. For example, an investor might consider that the increasing frequency and magnitude of drought in the Midwest poses a material risk to existing crop production and may lower productivity in the short- and potentially long-term, thus rendering some investments less appealing. Investors must be equipped with the tools and information to consider financially material factors like these when making investment decisions, or risk missing insights that can help deliver optimized risk-adjusted returns for their clients.

---

[4] PRI, Introductory Guides to Responsible Investment: What is responsible investment? (2022), available at: https://www.unpri.org/introductory-guides-to-responsible-investment/what-is-responsible-investment/4780.article.

[5] PRI, Top academic resources on responsible investment (July 2023), available at: https://www.unpri.org/research/top-academic-resources-on-responsible-investment/4417.article.

Rather than reflecting political bias, consideration of ESG factors becoming a fundamental part of investment practice is evidence of free markets working. ESG integration allows investors to incorporate insights into how companies are considering and responding to issues that can materially impact their success, both over the short and long-term. For example, the shift in investment flows from a carbon-intensive to a low-carbon economy represents both investment risk and opportunity, in terms of stranded assets and emergence of new technologies. Investors failing to respond to these changes risk missing out on potentially material insights and may be violating their fiduciary duties.[6]

Investors Require Access to Tools

Responsible investment practices—including ESG integration—are a necessary evolution of investment practice in response to new knowledge (like the evidence of the rapid advancement of impacts from human-caused climate change) and client demand. Fiduciary duties require investors to build new tools and develop new processes to accurately assess potentially material information.

Efforts to limit how investors can independently consider information can prove costly by imposing administrative burdens, limiting an investor's window into financial markets and narrowing the investible universe.[7] Vague guidelines can also create additional liability as one person's interpretation of "pecuniary", for example, can differ from the next.[8] Differing interpretations of what information is material is not an issue to be resolved, but rather the foundation of competitive financial markets where investors compete for better insights from combinations of information that provide better assessments, and better returns. As such, efforts to restrict or otherwise influence what information investors consider can have broad, unintended consequences on market efficiency, valuations and returns.

Introducing new vague or weighted language can be seen as an attempt to interfere with investor decision-making; to underweight or ignore material information, or artificially limit investment timeline or scope.[9] This is reflected in the PRI[10] and 97% of public commenter support for the Department of Labor's proposed rulemaking, "Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights"[11] which removed "pecuniary" language from its regulations. It is also reflected in the vocal opposition from the professional investment community to similar efforts in state legislatures' 2023 sessions.[12] Instead, investors require the support of regulators and lawmakers as they work to fully assess potentially material information, in an objective way, to chart the best course of action for clients.

---

[6] David Atkin, PRI Blog: "Criticizing ESG incorporation does not make it any less essential (July 25, 2022), available at: https://www.unpri.org/pri-blog/criticising-esg-incorporation-does-not-make-it-any-less-essential/10282.article.
[7] Freedom to Invest, Economic Impacts (2023), available at: https://www.freedomtoinvest.org/economic-impacts.
[8] David H. Webber, David Berger, and Beth Young, Harvard Law School Forum on Corporate Governance, "The Liability Trap: Why the ALEC Anti-ESG Bills Create a Legal Quagmire for Fiduciaries Connected with Public Pensions (February 27, 2023), available at: https://corpgov.law.harvard.edu/2023/02/27/the-liability-trap-why-the-alec-anti-esg-bills-create-a-legal-quagmire-for-fiduciaries-connected-with-public-pensions/; and Karen Tyler, Commissioner, North Dakota Securities Department, comments before the North Dakota House Committee on Industry, Business and Labor (February 6, 2023), available at: https://video.ndlegis.gov/en/PowerBrowser/PowerBrowserV2/20230206/-1/2983.
[9] PRI, "Consultation Response: U.S. Department of Labor: Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights" (December 13, 2021), available at: https://dwfyzx5upklss.cloudfront.net/Uploads/g/n/i/pricommentin1210ac03_138307.pdf; and "Consultation Response: U.S. Department of Labor: Fiduciary Duties Regarding Proxy Voting and Shareholder Rights" (October 5, 2020), available at: https://dwfyzx5upklss.cloudfront.net/Uploads/d/h/r/pricomment_dolfiduciarydutiesproxyvotingandshareholderrightsim1210ap91_20966.pdf; and "Consultation Response: U.S. Department of Labor: Financial Factors in Selecting Plan Investments" (July 30, 2020), available at: https://dwfyzx5upklss.cloudfront.net/Uploads/f/n/b/pricomment_dolerisaproposedrule30july2020_98837.pdf.
[10] US SIF, "Blog: Public Comments Overwhelmingly Support US Labor Department Proposal To Allow ESG Considerations In Retirement Plans" (January 26, 2022), available at: https://www.ussif.org/blog_home.asp?display=182.
[11] U.S. Department of Labor, Employee Benefits Security Administration, "Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights – Proposed Rule" (October 13, 2021), available at: https://www.dol.gov/agencies/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AC03.
[12] Pleiades Strategy, "2023 Statehouse Report: Right-Wing Attacks on the Freedom to Invest Responsibly Falter in Legislatures" (2023), available at: https://drive.google.com/file/d/1138kmUxWFK43nCQxc-m_EbOADUkBcbPr/view.

Investors Require Access to Information

Transparency sits at the heart of responsible investment. The PRI advocates for increased disclosure of corporate and investor practices so the market can better assess the actions of market participants.

In response to the growing understanding of the materiality of ESG-related factors, investors require additional information from companies. A significant amount of ESG-related information is already known or easily compiled by companies. For example, energy and water bills provide a starting point for disclosing natural resource use. Employee demographic information is already compiled and reported to the Equal Employment Opportunity Commission but is not available publicly. In 2021, 96% of the S&P 500 and 81% of the Russell 1000 produced sustainability reports (up from 20% in 2011).[13]

Globally, financial markets continue to align on the material corporate ESG-related information they find most informative. This makes it easier for investors to gather the insights needed and more efficient for companies to disclose a consistent set of information in an increasingly comparable way.

For example, investor demand for climate-related information is increasingly aligned globally.[14] The IFRS Foundation—which sets accounting standards for 140 jurisdictions—recently published its draft baseline of climate-related disclosure which also draws from the US-founded Sustainability Accounting Standards Board (SASB) that merged with IFRS in 2022.[15] Additional efforts to establish baselines for other ESG-related issues are underway.[16] The SEC's proposed rule, "The Enhancement and Standardization of Climate-Related Disclosures for Investors"[17] aligns closely with the work of the IFRS Foundation and Taskforce on Climate-Related Financial Disclosures, among other global initiatives, and would support investor needs on material climate-related information.[18]

More broadly, the basic expectations for companies to protect human rights and operate responsibly were laid out more than a decade ago by the United Nations and OECD, respectively.[19] Just as ESG is not a new consideration for the financial sector, increased expectations for business conduct and related disclosure has been growing for decades. For example, the United Nations Global Compact (UNGC) has for more than 20 years sought to align businesses around 10 core principles of responsible business on human rights, labor, the environment and anti-corruption. UNGC has more than 1,000 signatories based in the United States.[20]

---

[13] Governance & Accountability Institute, Inc., "All-Time High of Sustainability Reports Among U.S. Publicly-Traded Companies" (2022), available at: https://www.ga-institute.com/research/ga-research-directory/sustainability-reporting-trends/2022-sustainability-reporting-in-focus.html.

[14] Task Force on Climate-Related Financial Disclosures, "TCFD Recommendations" (June 2017), available at: https://www.fsb-tcfd.org/recommendations/.

[15] IFRS Foundation, Climate-related Disclosures: "IFRS S2 Climate-related Disclosures" (June 26, 2023), available at: https://www.ifrs.org/projects/completed-projects/2023/climate-related-disclosures/#published-documents.

[16] Taskforce on Nature-related Financial Disclosures, "About", available at: https://tnfd.global/about/.

[17] U.S. Securities and Exchange Commission, "The Enhancement and Standardization of Climate-Related Disclosures for Investors", (April 11, 2022), available at: https://www.federalregister.gov/documents/2022/04/11/2022-06342/the-enhancement-and-standardization-of-climate-related-disclosures-for-investors.

[18] PRI, "Consultation Responsible: Securities and Exchange Commission File No. S7-10-22: The Enhancement and Standardization of Climate-Related Financial Disclosures for Investors" (June 17, 2022), available at: https://dwtyzx6upklss.cloudfront.net/Uploads/s/d/z/pricomment_secclimaterelateddisclosures_423012.pdf; and PRI signatory letter on the SEC's Request for Comment on Climate Change Disclosure (June 11, 2021), available at: https://dwtyzx6upklss.cloudfront.net/Uploads/g/q/m/pridisclosuresignatoryletter_15524.pdf; and PRI signatory letter to SEC Chair Gensler on the proposed rule (November 1, 2022), available at: https://dwtyzx6upklss.cloudfront.net/Uploads/h/o/i/priletter_climatedisclosureruleflegal_480085.pdf.

[19] United Nations, Office of the High Commission on Human Rights, "Guiding Principles on Business and Human Rights" (2011), available at: https://www.ohchr.org/sites/default/files/documents/publications/guidingprinciplesbusinesshr_en.pdf; and OECD, "OECD Guidelines for Multinational Enterprises on Responsible Business Conduct (September 29, 2011, updated June 8, 2023), available at: https://mneguidelines.oecd.org/mneguidelines/.

[20] United Nations Global Compact (2023), available at: https://unglobalcompact.org/.

The PRI similarly supports disclosure from investors and the financial sector. Since its launch in 2006, the PRI has grown into the largest responsible investment reporting initiative globally with thousands of investors completing the Reporting Framework annually.[21] The Reporting Framework provides transparency and accountability on signatory responsible investment practices, allowing investors, clients and the market to compare practices year-over-year. The PRI continuously looks to improve the reporting process to be more efficient for reporters and useful for the market.

Progress continues to be made in efforts to provide retail investors, asset owners and market participants better disclosure from investment managers and funds. In 2022, the SEC finalized improvements to Form N-PX, the annual form required by all investment funds detailing proxy voting activities.[22] These improvements made the proxy voting process more transparent, providing more consistent and comparable data in a searchable, accessible, organized and efficient format.[23]

Further, the PRI supports the SEC's proposed rule "Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social, and Governance Investment Practices"[24] to address greenwashing by improving the information provided by investment managers. This will support retail investors to better understand the products they are purchasing.[25] The PRI similarly supports the SEC's proposed amendments to the Investment Company Names rule to ensure a fund's name—the most prominent disclosure of a fund—matches the underlying assets within that fund. These proposals seek to ensure that investment manager activities reflect their accompanying public disclosures; essentially, that investors know what their managers are doing on their behalf.[26] These improvements represent the natural, and necessary, evolution of the SEC's disclosure regime designed to, primarily, protect investors and, secondarily, maintain fair, orderly and efficient markets.[27]

---

[21] PRI, The Reporting Process, "Investor Reporting Framework" (24 May 2023), available at: https://www.unpri.org/reporting-and-assessment/investor-reporting-framework/3373.article.
[22] U.S. Securities and Exchange Commission, "Final Rule: Enhanced Reporting of Proxy Votes by Registered Management Investment Companies; Reporting of Executive Compensation Votes by Institutional Investment Managers" (November 2, 2022), available at: https://www.sec.gov/rules/final/2022/33-11131.pdf.
[23] PRI, "Consultation Response: Enhanced Reporting of Proxy Votes by Registered Management Investment Companies; Reporting of Executive Compensation Votes by Institutional Investment Managers; File Number S7-11-21" (December 14, 2021), available at: https://dwtyzx8upkiss.cloudfront.net/Uploads/w/wc/priconsultation_formnpx_443144.pdf.
[24] U.S. Securities and Exchange Commission, "Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social, and Governance Investment Practices", (June 17, 2022), available at: https://www.federalregister.gov/documents/2022/06/17/2022-11718/enhanced-disclosures-by-certain-investment-advisers-and-investment-companies-about-environmental.
[25] PRI, "Consultation Response: Securities and Exchange Commission File No. S7-17-22: Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social, and Governance Investment Practices" (August 16, 2022), available at: https://dwtyzx8upkiss.cloudfront.net/Uploads/b/o/x/pribinaladviserfunddisclosureubs_973483.pdf.
[26] PRI, "Consultation Response: Securities and Exchange Commission File No. S7-16-22: Investment Company Names" (August 16, 2022), available at: https://dwtyzx8upkiss.cloudfront.net/Uploads/b/o/x/bindnamerequle_pri_secfilemo_s71622_788543.pdf.
[27] U.S. Securities and Exchange Commission, "About the SEC" (April 6, 2023), available at: https://www.sec.gov/strategic-plan/about.

Shareholder Rights Must Be Protected

The rights attributed to shareholders in public companies are the core agreement that drives US financial markets—the deepest and most liquid in the world.[28] Investors exercise their rights as shareholders on material ESG-related issues in the same way, and for the same reasons, they exercise these rights on other issues: to encourage high standards of performance in the companies and entities in which they invest as part of a long-term investment strategy. Their enhanced scrutiny of corporate management on ESG risks and opportunities stems from the fundamental desires of investors to protect value and maximize risk adjusted returns.

The concerns raised by the ESG Working Group[29] regarding shareholder rights—specifically the proxy voting process—reiterate those proffered by the SEC in 2020 in its rulemakings, "Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a-8"[30] and "Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice".[31]

The PRI opposed both above referenced proposals as they were built upon similar inaccurate assessments of the proxy voting process.[32] Voting proxies is an effective tool that investors use to engage with investee company management and to share views and expectations. Many institutional investors recognise proxy voting as part of their fiduciary duty to clients because it can be used to influence corporate behavior, and thus, returns.

The SEC's changes to Rule 14a-8 made it more difficult for shareholders to submit proxies for a vote despite evidence that the rule would disproportionately harm retail investors, those traditionally least able to have their views heard.[33] As the underlying owners of corporate entities, shareholders should maintain the ability to engage with management on material issues and to escalate those engagements to public votes when deemed necessary.[34]

Similarly, as the PRI stated to the SEC in 2020, "proxy advisory firms conduct the important and necessary work of providing high quality, independent analyses, linking [analysis] to voting recommendations based on institutional investors' stated priorities. Many institutional investors use proxy advisory firms' recommendations to supplement their research and understanding of multiple, detailed, and sometimes dense proxies for their portfolio."[35] Efforts to interfere with this customer-client relationship would limit the important market efficiencies gained by these services and impose increased costs on investment managers least able to afford them.

---

[28] SIFMA, "Research Quarterly: Equities" (April 28, 2023), available at: https://www.sifma.org/resources/research/research-quarterly-equities/#:~:text=The%20U.S.%20equity%20markets%20are,the%20next%20largest%20market%2C%20China.

[29] ESG Working Group, House Committee on Financial Services. "Preliminary Report on ESG Climate Related Financial Services Concerns" (June 23, 2023), available at: https://financialservices.house.gov/uploadedfiles/hfsc_esg_wg_group_memo_final.pdf.

[30] U.S. Securities and Exchange Commission, "Procedural Requirements and Resubmission Thresholds Under Exchange Act Rule 14a-8" (November 4, 2020), available at: https://www.federalregister.gov/documents/2020/11/04/2020-21580/procedural-requirements-and-resubmission-thresholds-under-exchange-act-rule-14a-8.

[31] U.S. Securities and Exchange Commission, "Exemptions From the Proxy Voting Rules for Proxy Voting Advice" (September 3, 2020), available at: https://www.federalregister.gov/documents/2020/09/03/2020-19337/exemptions-from-the-proxy-rules-for-proxy-voting-advice.

[32] PRI, Letter from PRI, select signatories and supporting organizations on "File numbers: S7-23-19; S7-22-19" (February 3, 2020), available at: https://d8g8t13e9vf2o.cloudfront.net/Uploads/q/n/l/sec-pri-letter_pri_february3_2020_907635.pdf.

[33] PRI, et al. "Letter Re: Improper Exclusion of Evidence on the Impact of the Proposed Amendments to Rule 14a-8 on Retail Investors" (September 4, 2020), available at: https://dwtyzx6upklss.cloudfront.net/Uploads/x/u/cvgroupcommentletteronimproperlyexclusionofevidenceonimpactonretailinvestors_136927.pdf.

[34] PRI, "File Number: S7-23-19: Proposed Rule: Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a-8" (February 3, 2020), available at: https://d8g8t13e9vf2o.cloudfront.net/Uploads/g/h/l/pris723192_february032020_88213a.pdf.

[35] PRI, "File Number S7-22-19: Proposed Rule: Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice" (February 3, 2020), available at: https://d8g8t13e9vf2o.cloudfront.net/Uploads/g/h/l/pris722192_february032020_623133.pdf.

Like any third-party recommendation to an independent business, it is up to that business to determine when and how to utilize the third-party advice to achieve its goals. Investment managers are ultimately responsible for conducting due diligence on third-party advisory services and ensuring their proxy voting policies are implemented correctly.

Progress has been made on better serving shareholders in the proxy voting process with the approval of the SEC's requirement of universal proxy cards. Universal proxies will ensure that shareholders have equal access to the full slate of candidates for director positions.[36] We should look toward similar efforts as this where efficiencies can provide better information to market participants and support the underlying purpose of capital markets: to provide long-term, sustainable returns for investors.

Should you or any members of the Committee like to discuss these comments further or how the PRI can support your work on other issues, please do not hesitate to contact our policy team at policy@unpri.org.

Sincerely,

David Atkin

Chief Executive Officer, Principles for Responsible Investment

[36] PRI, "Consultation Response: Securities and Exchange Commission: Reopening of Comment Period on Universal Proxy" (June 7, 2021), available at: https://www.sec.gov/comments/s7-23-19/s72319-8892483-244...

Statement for the Record by
Sanford Lewis, Director and General Counsel
Shareholder Rights Group

For the Hearings on ESG Before the
House Financial Services Committee
U.S. House of Representatives

Regarding Hearings of July 12 and 13
***Reforming the Proxy Process to Safeguard Investor Interests* and**
Protecting Investor Interests: Examining Environmental and Social Policy in Financial Regulation

I am grateful for the opportunity to offer this statement on behalf of the Shareholder Rights Group to the House Financial Services Committee ("the Committee"). The Shareholder Rights Group is an association of individual and institutional investors defending the rights and freedoms of investors to protect their investments. This statement reflects my own opinion as Director.

The Securities and Exchange Commission (SEC) shareholder proposal rule ("Rule 14a-8" or "the rule") has proven to be one of the most critical shareholder rights for investors, retail and institutional alike, to protect their investments. Shareholders file proposals to ensure that companies are appropriately managing risk and disclosing the information investors need to inform investment decision-making and conduct adequate due diligence. Generally, investors file proposals to improve governance, increase transparency on issues relevant to investors, and to ensure that corporate leadership is acting in alignment with investors' long-term interests. As such, the rule is aligned with the SEC's mission to protect investors from, among other things, fraud, an unlevel informational playing field, and the extraction of private benefits from the firm by firm insiders.[1]

The rights to file and vote upon shareholder proposals are a keystone of American capitalism and corporate governance. While the Commission and Staff have fine-tuned the rule over the years, attempts to curtail shareholder rights have arisen every decade since the rule was promulgated more than 80 years ago. Prudently, these efforts have mostly been rejected by the Commission as well as Congress.[2]

---

[1] https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2282103

[2] An exception was the 2020 rulemaking promulgated by the Commission which has significantly raised filing and resubmission thresholds. In 2020, the Commission, responding to comments from issuers, adopted new steeper thresholds for filing and resubmission of shareholder proposals. The prior rule allowed any shareholder with over $2000 in company shares held for at least a year to file a proposal; the new rule increased the required "skin in the game" by requiring that if the shareholder only held shares for a year they would need to hold at least $25,000 in shares; smaller shareholders holding only $2,000 are now required to hold their shares for at least three years before filing a proposal. The thresholds to resubmit a proposal in subsequent years after a vote were also raised significantly. The prior rule required 3% voting support on a first vote, 6% on a second vote and 10% on a third year and subsequent votes. In contrast the new rule requires 5% the first year, 15% the second year and 25% the third year.

We urge all Committee members to respect the well-honed dynamics of the capital markets and the SEC's administration of Rule 14a-8, and therefore to reject proposed legislative changes that would undercut these fundamental shareholder rights.

About the Shareholder Proposal Rule

The shareholder proposal rule is grounded in the recognition that a company's annual meeting is a crucial forum for companies–to provide transparency on certain important issues– and for investors–to elect directors and to advise the board and management on significant issues facing the company. It is a well-established and predictable process that provides significant benefits to companies and investors. Currently, there are procedural and substantive requirements that screen out inappropriate shareholder proposals, and require proponents to hold sufficient stake to merit their proposals' consideration. As a result, legislative reforms are unnecessary and would be disruptive.

The shareholder proposal process provides important benefits to public companies and is not a significant burden.

Over the last 80 years, the SEC shareholder proposal rule has encouraged many companies to adopt governance and disclosure policies that are today considered corporate best practice:

- Norms that improved accountability of directors, such as independent directors constituting a majority of the board and the annual election of directors by majority vote;

- Corporate disclosures that allow investors to assess and manage investment risks and evaluate a company's resilience and sustainability into the future, for example its management of issues such as climate risk and boardroom diversity.

The Right of Shareholders to Engage on Issues of Consequence for Their Companies Must Be Protected

Although some members of the Committee have questioned whether shareholder proposals on environmental or social issues are appropriate for corporate annual meetings, it is a foundational and a long-standing right of shareholders to raise important issues of public debate or impact relevant to the future of their company.

There is no question as to whether corporations are impacted by social and environmental issues. By virtue of their resources and actions, corporations inherently *do* make decisions with significant social and environmental consequences and are also impacted by changing social dynamic and the environmental conditions within which they operate.

Rather, the question being asked is *who* deserves a voice in such decisions. Ultimately, boards and managers will make consequential choices, but the law provides that companies should not be insulated from valuable shareholder feedback and advice that is, in part, facilitated by the shareholder proposal process. The DC Circuit Court has made it clear that silencing shareholders on such issues cannot "be harmonized with the philosophy of corporate democracy"

embodied in federal law.[3]

In respect of the role and discretion of management and board in running companies, SEC rules exclude proposals that merely address the day-to-day management of a corporation. In contrast, shareholders maintain a fundamental right to file and vote upon proposals on emerging issues relevant to the company's future.

Ultimately, the rule allows shareholders to express their voice and opinions through voting. Well conceived proposals, compliant with SEC rules, are able to reach the proxy statement, but the ultimate test is the proxy statement as a *marketplace of ideas.* Significant voting support for a shareholder proposal is dependent upon investors' understanding of whether the subject matter may affect value for investors, especially over longer time horizons.

Social and environmental proposals raise critical investor risk management concerns and often provide an early warning of issues that may ultimately prove to be highly material and even existential to a company.

To take one example: a 2013 shareholder proposal filed by the New York City Comptroller at Wells Fargo encouraged the company to establish a policy to recoup pay from executives whose conduct caused financial or reputational harm to the company. The proposal was never voted upon, because the company agreed to make the change after the proposal was filed. As a result, after the company settled charges in 2016 that it had improperly created 3.5 million unauthorized accounts, more than $180 million was clawed back from executives for failure to sufficiently prevent these problems.[4]

Proposals on climate risk are on a similar footing. A large portion of the market believes that climate change represents a significant financial risk, even an existential risk, to companies and the economy. Businesses will be transformed by the decarbonization of the economy and efforts to improve climate disclosure and performance are aligned with investor interests. Investors employ the shareholder proposal process to better understand how a company is evaluating and mitigating climate risks; for example, filing a proposal requesting companies to disclose its plans to address the physical and transitional risks presented by climate change. The economic risks to future retirees from corporate inaction to address climate risk is substantial. For instance, Swiss Re's stress testing estimates that global GDP may be between 4% and 18% lower by 2050, depending on how successful we are in reducing GHG emissions. Efforts to block climate risk related shareholder proposals essentially attempt to force investors to invest as if climate change is not happening, and to ignore the risks to their companies and to the economy writ large. That is a dangerous and costly proposition.

The only mandatory cost associated with the shareholder proposal rule is for the issuer to publish a proposal limited to no more than 500 words in the proxy. In contrast to these minimal printing costs, the issues elevated by shareholder proposals, including environmental or social

---

[3] *Medical Comm. for Human Rights v. SEC*, 432 F.2d 659, 680-81 (D.C. Cir. 1970).

[4] The New York Times has noted that prior attempts to roll back shareholder proposal rights would have blocked the clawback proposal. https://www.nytimes.com/2017/06/16/business/wells-fargo-clawback-fair-choice-act-shareholders.html

proposals, often reflect risks that could amount to billions of dollars of liability or reputational damage, or alternatively, opportunities with the potential for increased profitability. The value of the shareholder proposal process to companies and their investors far exceeds the cost.

The Commission has responded to Company and Investor Feedback and the Process is Now Efficient and Predictable for All

The Commission's ordinary business rule, Rule 14a-8(i)(7), allows companies to exclude shareholder proposals focusing only on the day-to-day operations of the corporation. Such day-to-day decision-making is reserved to the discretion of the board and management. Shareholder proposals are reserved for the significant issues facing a company, which is why SEC rules and Staff guidance do not allow exclusion of shareholder proposals raising significant policy issues.

During the Trump administration, the Staff issued three staff legal bulletins (subregulatory guidance) that provided new tests for interpreting ordinary business. These tests allowed companies opportunities to raise additional objections for potentially excluding a proposal, and thereby introduced *subjective* opportunities for SEC staff to allow exclusion.[5]

Under Chair Gensler, the Commission's staff issued Staff Legal Bulletin 14L, which repealed the subjective criteria for ordinary business added during the preceding years, and focused the question of a "significant social policy issue" on whether a proposal addresses an issue of significant social impact. The change aligns with the interests of shareholders as it has become clear that issues of major social or environmental impact are likely to affect a company's bottom line in the near- or long-term and can impact the prospects for diversified investors in the broader economy whose portfolio-wide value can be significantly undercut by externalities.[6]

Because of Staff Legal Bulletin 14L, issuers and proponents have greater predictability as to whether or not the SEC will exclude a particular proposal. In 2023, we estimate that this resulted in a 30% drop in no-action challenges by issuers, which represents a reduction in costs to companies and investors associated with those challenges. More predictability means that shareholders can ensure proposals are in compliance with the rules, and issuers save money by not spending corporate funds on subjective and highly debatable legal challenges. Despite claims that the Staff Legal Bulletin 14L opened the floodgates for proposals, this year the Staff continued to allow exclusion of proposals based on companies' ordinary business and micromanagement assertions in no action requests.[7]

---

[5] For example, the Staff sought out the opinion of the company's Board of Directors (in addition to their lawyers) as to whether or not the proposal addressed ordinary business, and offered multiple new avenues and hooks for companies to argue ordinary business on almost any proposal. This resulted in proliferation of lengthy no action requests prepared by company lawyers attempting to fulfill the extensive criteria set forth by the Staff.

[6] Judicial and Commission interpretations affirm that shareholders have a legitimate and compelling interest in being heard on these matters. As the D.C. Circuit Court of Appeals has noted, "the clear import of the language, legislative history, and record of administration of section 14(a) is that its overriding purpose is to assure corporate shareholders the ability to exercise their right — some would say their duty — to control" important corporate decisions. *Medical Comm. for Human Rights v. SEC*, 432 F.2d 659, 680-81 (D.C. Cir. 1970).

[7] Corporate lawyer Marc Gerber discussed this trend in exclusion of numerous proposals this year in a recent blog post. https://corpgov.law.harvard.edu/2023/07/08/shareholder-proposal-no-action-requests-in-the-2023-proxy-season/

We have heard outsized and exaggerated claims that the number of shareholder proposals facing companies is massively expanding. At most, about 20% more shareholder proposals reached corporate proxy statements in 2023. In the context of the broader market, that is not a significant increase. The majority of public companies still do not receive any shareholder proposals. On average, 13% of Russell 3000 companies received a shareholder proposal in a particular year between 2004 and 2017. In other words, the average Russell 3000 company can expect to receive a shareholder proposal once every 7.7 years. For companies that receive a shareholder proposal, the median number is one per year.[8]

In short, the shareholder proposal rule is functioning as intended. There is not an explosion of inappropriate shareholder proposals as a result of the new staff legal bulletin, but instead clarity for investors seeking to protect their assets.

Legislative Reforms Are Unnecessary and Would Disrupt Capital Market Relationships

We note that the Committee is set to consider numerous examples of legislation that would significantly diminish shareholder rights and should therefore be of grave concern to all shareholders and fiduciaries.

Some of the legislative proposals would allow issuers to write their own bylaws governing the types of shareholder proposals that could be considered at a company's annual meetings. Setting aside the question of whether companies would do so over the objections of shareholders, it should be evident that transforming what is currently an efficient and time-tested set of rules into a complicated web of company bylaws would neither be in investor or company interests. It could well divert shareholder concerns into more disruptive fights including books and records requests, shareholder litigation, "vote no" campaigns and contested Director elections.

I want to briefly address another concept highlighted in the preliminary committee report on ESG which inaccurately states that the SEC eliminated "the requirement for proposals to be relevant to a company's business."[9] To the contrary, shareholder proposals are required to be relevant to companies, and are excludable if they are not. The existing and continuing relevance rule, Rule 14a-8(i)(5), permits a company to exclude a proposal if it relates to operations which account for less than five percent of the company's total assets at the end of its most recent fiscal year, and for less than five percent of its net earnings and gross sales for its most recent fiscal year, and is not otherwise significantly related to the company's business. An activity that might comprise a minor part of the company's business financially is still "significantly related" to the company's business if the activities in question pose a threat to the company in other ways.

Much has been made of the staff legal bulletin's elimination of the "nexus" test. "Nexus" refers to a vague and redundant relevance test added by SEC staff that went far beyond the rules established by the Commission **that already require a proposal be *relevant* to a company**. The nexus concept attempted to further probe the relevance of a social policy issue to a company; in

---

[8] Council of Institutional Investors, "Frequently Asked Questions about Shareholder Proposals" Accessible at: https://www.cii.org/files/10_10_Shareholder_Proposal_FAQ(2).pdf

[9] ESG Working Group, House Committee on Financial Services "Preliminary Report on ESG Climate Related Financial Services Concerns," Page 15, (June 23, 2023) accessible at: https://financialservices.house.gov/uploadedfiles/hfsc_esg_working_group_memo_final.pdf

reality, the nexus test has neither good grounding in the Commission's promulgated rules and releases, nor any objective means of determination.[10] From the standpoint of investors, the removal of the subjective, nexus test in Staff Legal Bulletin 14L constituted welcome relief, and enhanced the ability of proponents to predictably draft proposals that would meet the criteria of the rule and avoid exclusion.[11]

In short, the existing relevance rule is functional and recommendations to restore a nexus or materiality test amount to recommendations to fix something that isn't broken, and serving only to reintroduce subjectivity and unpredictability to SEC staff decision making.

Conclusion

Shareholder democracy is part of the fabric of American capitalism. In our free enterprise system, investors have the freedom to take risks to grow and sustain their investments, supported by essential rights in the governance of corporations. Shareholder proposals are a time tested, fundamental right of shareholders to hold investee boards and managers accountable on the issues that investors believe will matter for the long term. The resultant dialogue, engagement, education and reforms are a source of vigor and dynamism for American corporations.

I would expect that few legislators of any political orientation would knowingly support "reforms" that would curtail the rights and freedoms of retail and institutional shareholders. Nor would they knowingly attempt to substitute political judgments for the analytical processes of professionals in the financial markets.

The affected investors appreciate your thoughtful and judicious attention to these issues, and urge you to avoid support for legislative initiatives which appear as a "solution" in search of a problem.

---

[10] https://corpgov.law.harvard.edu/2021/12/23/sec-resets-the-shareholder-proposal-process/ The nexus rule promoted the proliferation of complex company no-action challenges, spawning an opportunity for companies to make extended subjective and philosophical arguments to the SEC staff regarding the absence nexus.

[11] Clearly, the existing relevance rule continues to apply and to bear on the types of issues that are being raised as a cause for bringing back "nexus". A proposal that merely seeks a general corporate plebiscite on a social or ethical issue on which the company has no impact or involvement would be unlikely to pass the Rule 14a-8(i)(5) test of being "otherwise significantly related to the company's business".

July 18, 2023

The Honorable Patrick McHenry
Chair
Committee on Financial Services
U.S. House of Representatives
2129 Rayburn House Office Building
Washington, DC 20515

The Honorable Maxine Waters
Ranking Member
Committee on Financial Services
U.S. House of Representatives
2221 Rayburn House Office Building
Washington, DC 20515

The Honorable Ann Wagner
Chair
Subcommittee on Capital Markets
U.S. House of Representatives
2350 Rayburn House Office Building
Washington, DC 20515

The Honorable Brad Sherman
Ranking Member
Subcommittee on Capital Markets
U.S. House of Representatives
2181 Rayburn House Office Building
Washington, DC 20515

Dear Chairs McHenry and Wagner and Ranking Members Waters and Sherman:

The undersigned organizations would like to take this opportunity to submit the following comment on the hearing entitled, "Oversight of the SEC's Division of Corporation Finance."

We know that farmers and ranchers of all sizes are increasingly taking advantage of significant business opportunities and financial incentives for sustainable agricultural practices and products—many of which attract new customers, green premiums, and new investment.

However, we are concerned that some members of this committee have made misleading claims[1] that the Securities and Exchange Commission's proposed rule for Enhancement and Standardization of Climate-Related Disclosures for Investors (RIN 3235-AM87) would cause substantial burdens to farmers. These harmful claims promote messaging from agribusiness companies and their lobby,[2] undermine corporate disclosure requirements,[3] and distract from the

[1] "Congressman Lucas Introduces Bill Excluding Agriculture from SEC Climate Disclosure Rulemaking," September 29, 2022. https://lucas.house.gov/posts/congressman-lucas-introduces-bill-excluding-agriculture-from-sec-climate-disclosure-rulemaking

[2] Myers, Shelby. "Overreach of SEC Proposed Climate Rule Could Hurt Agriculture." *American Farm Bureau Federation*, May 6, 2022. https://www.fb.org/market-intel/overreach-of-sec-proposed-climate-rule-could-hurt-agriculture and Comments by National Agricultural Associations on SEC's Proposed Rules on the Enhancement and Standardization of Climate-Related Disclosures for Investors (File No. S7-10-22) , June 17, 2022. https://www.sec.gov/comments/s7-10-22/s71022-20132020-302492.pdf. Texas Farm Bureau. "Bill introduced to block greenhouse gas disclosures." May 23, 2023. https://texasfarmbureau.org/bill-introduced-to-block-greenhouse-gas-disclosures/

[3] Institute for Agriculture and Trade Policy, "Agribusiness opposition to the proposed SEC climate-related financial disclosure rule," August 12, 2022. https://www.iatp.org/agribusiness-opposition-proposed-sec-rule

real material risk that climate change—not climate disclosure—poses to our members' lives and livelihoods.

This letter provides an overview of the current challenges in industrial agriculture as a result of market consolidation and how climate financial risk harms not just investors, but other critical stakeholders, including farmers, farm workers, and consumers. Members of this committee have invoked concern for these stakeholders as grounds to oppose a robust climate-disclosure rule, so it is important to hear from groups like ours that represent these constituencies rather than only the industrial farm lobby.

Risk to Farmers

Ongoing climate-related physical risks, from torrential downpours to prolonged droughts, have left farmers across the country reeling. Due to erratic weather patterns and temperature spikes and drops, many farmers are being forced to change the types of crops they plant or even abandon their crops altogether. In 2022, cotton farmers in Texas abandoned 74 percent of their planted crops due to extreme heat and drought.[4] Ninety-five percent of the state was in a drought in July of that year.[5] California produces nearly 75 percent of the nation's fruits and nuts, both of which are extremely vulnerable to climate change, and severe drought also forced California farmers to abandon large portions of their almond crops.[6] These devastating conditions are forcing farmers to make hard choices to keep their businesses financially solvent especially as climate risks continue to grow.

An annual survey of Iowa farmers conducted in 2020 found that more than half (51%) of farmers agreed with the statement, "I am concerned about the potential impacts of climate change on my farm operation."[7] In Montana, a state where climate change is projected to cost 25,000 jobs and $736 million in losses over the next 50 years,[8] nearly three quarters of farmers and ranchers

---

[4] Coral Davenport, "How Climate Change Is Making Tampons (and Lots of Other Stuff) More Expensive," *The New York Times*, February 18, 2023, https://www.nytimes.com/2023/02/18/climate/climate-change-cotton-tampons.html.
[5] Dalia Faheid, "Texas Drought Is the Worst in Years | Fort Worth Star-Telegram," *Forth Worth Star-Telegram*, July 22, 2022, https://www.star-telegram.com/news/state/texas/article260135445.html, and Jayme Lozano Carver, "Texas' Cotton Industry Is Facing Its Worst Harvest in Years - Costing the State More than $2 Billion," *The Texas Tribune*, August 31, 2022, https://www.texastribune.org/2022/08/31/texas-drought-cotton-farming-economy/.
[6] Elizabeth Elkin, "California Drought Is Withering Almond, Dairy Farms in Food Inflation Threat," *Bloomberg*, June 23, 2021, https://www.bloomberg.com/news/features/2021-06-23/california-drought-is-withering-almond-dairy-farms-in-food-inflation-threat?sref=f7rH2jWS.
[7] J. Gordon Arbuckle Jr., "Iowa Farm and Rural Life Poll Shows Farmers' Beliefs on Climate Change Are Shifting," *Iowa State University*, January 22, 2021, https://www.extension.iastate.edu/news/iowa-farm-and-rural-life-poll-shows-farmers-beliefs-climate-change-are-shifting.
[8] Thomas Michael Power and Donovan S Power, "The Impact of Climate Change on Montana's Agriculture Economy," *E&E News*, February 16, 2022, https://legacy-assets.eenews.net/open_files/assets/2017/07/03/document_gw_01.pdf.

surveyed reported experiencing "moderate to high levels of anxiety when thinking about climate change and its effects on their agricultural business."[9] And a 2021 survey from the American Farm Bureau Federation found that drought conditions yielded less crops and changed farming practices of farmers and ranchers.[10]

Farmers are also exposed to indirect impacts of climate financial risks, including loss of credit, negative physical and mental health, and lower home values. These risks are further magnified by the devastating trendline of consolidation in the agriculture sector.

Risk to Farm Workers

Farm workers labor under extreme conditions that are exacerbated by climate change—including harvesting crops when temperatures exceed 100 degrees Fahrenheit with minimal access to clean drinking water, and inhaling toxic air pollution from wildfire smoke—to ensure that Americans are fed, often at great danger to themselves. Farm workers when compared to other workers are 35 times more likely to die from illnesses caused by heat-related stress.[11] A survey of farm workers in Washington state found that nearly 75 percent were exposed to an unhealthy amount of wildfire smoke while working and 100 percent reported that they had little or no information about how to protect themselves from the smoke.[12]

But the vulnerability of farm workers extends beyond their physical working conditions. Nearly half of farm workers are undocumented and struggle with challenges around immigration and language barriers.[13] They also face financial insecurity, which will only worsen as climate disasters increase in severity and frequency.

---

[9] "Three-Quarters of Montana Farmers, Ranchers Anxious about Climate Change, Survey Finds " Yale Climate Connections," *Yale Climate Connections*, July 14, 2022, https://yaleclimateconnections.org/2022/07/montana-farmers-ranchers-anxious-about-climate-change-survey-finds.

[10] Daniel Munch, "New AFBF Survey Shows Drought's Increasing Toll on Farmers and Ranchers," *American Farm Bureau Federation*, August 14, 2022, https://www.fb.org/market-intel/new-afbf-survey-shows-droughts-increasing-toll-on-farmers-and-ranchers.

[11] Moussa El Khayat et al., "Impacts of Climate Change and Heat Stress on Farmworkers' Health: A Scoping Review," *Frontiers in public health*, February 8, 2022, https://www.ncbi.nlm.nih.gov/pmc/articles/PMC8861180/#:~:text=In%2520fact%252C%2520occupational%2520heat%252d Related,standards%2520(23%25E2%2580%259325).

and Melina Walling, "Climate Change Ratchets up the Stress on Farmworkers on the Front Lines of a Warming Earth," *Los Angeles Times*, July 8, 2023, https://www.latimes.com/world-nation/story/2023-07-08/climate-change-ratchets-up-the-stress-on-farmworkers-on-the-front-lines-of-a-warming-earth.

[12] "Wildfire Smoke Safety," *DEOHS*, accessed July 15, 2023, https://deohs.washington.edu/pnash/wildfiresmoke.

[13] Raquel Rosenbloom, "A Profile of Undocumented Agricultural Workers in the United States," *The Center for Migration Studies of New York (CMS)*, February 14, 2023, https://cmsny.org/agricultural-workers-rosenbloom-083022/#:~:text=Immigrants%20coming%20from%20Mexico%20comprise,percent. and "Immigrant Farmworkers and America's Food Production - 5 Things to Know," *FWD.us*, September 14, 2022, https://www.fwd.us/news/immigrant-farmworkers-and-americas-food-production-5-things-to-know/, and "Farm Labor," *USDA ERS*, accessed July 15, 2023, https://www.ers.usda.gov/topics/farm-economy/farm-labor/.

The seasonality of their occupation, low pay—often paid by a piece rate—and increasing climate disasters that disrupt work days and crop viability make farm workers particularly financially vulnerable. In 2022, the average family income for farm workers was between $25,000 and $29,999.[14]

Consolidation Impacts

The interests and realities for small farmers and farm workers should not be mistaken for the interests of agribusiness. Agribusiness consolidation touches upon every aspect of the agriculture industry, from seeds to farm equipment.[15] Today, just four companies—Cargill, Tyson Foods Inc., JBS SA, and National Beef Packing Co.—control a staggering 70 percent of the U.S. beef market.[16] Over seventy percent of the global grain trade is controlled by four companies: Archer Daniels Midland (ADM), Bunge, Cargill, and Louis Dreyfus Company.[17] Farmers largely purchase their grain from these four companies since they wield tremendous influence over the markets and there is little government policy development to break up their market concentration power. Tyson Foods Inc, ADM, and Bunge would be required to disclose their *estimated* emissions under the SEC's proposed rule.

This level of consolidation creates barriers to entry for new farmers, who are often young, come from non-farm backgrounds, and lack access to land,[18] making it difficult for new farmers to join the field despite the agricultural sector's dire need to train the next generation of farmers as the majority near retirement. Farmers over the age of 65 outnumber farmers under the age of 35 by more than six to one.[19]

---

[14] Alice Reznickova, "How Many Farmworkers Are Food Insecure? It's Hard to Tell," *Union of Concerned Scientists*, May 26, 2023, https://blog.ucsusa.org/alice-reznickova/how-many-farmworkers-are-food-insecure/.
[15] Billy Hackett, "Farmers Trapped in Unsustainable Cycle by Biotechnology, Seed Consolidation," *National Sustainable Agriculture Coalition*, July 20, 2021, https://sustainableagriculture.net/blog/farmers-trapped-in-unsustainable-cycle-by-biotechnology-seed-consolidation, and "'hog-Tied' and Fed up: New Report Shows Dealership Consolidation Makes Farmers' Lives Harder." *PIRG*, March 2, 2022. https://pirg.org/media-center/hog-tied-and-fed-up-new-report-shows-dealership-consolidation-makes-farmers-lives-harder/.
[16] "Explainer: How Four Big Companies Control the U.S. Beef Industry," *Reuters*, June 17, 2021, https://www.reuters.com/business/how-four-big-companies-control-us-beef-industry-2021-06-17/.
[17] Sophia Murphy, David Burch, and Jennifer Clapp, "Cereal Secrets: The World's Largest Grain Traders and Global Agriculture ," *Oxfam*, August 2012, https://oxfamilibrary.openrepository.com/bitstream/handle/10546/237131/rr-cereal-secrets-grain-traders-agriculture-30082012-en.pdf?sequence=10. and Felicity Lawrence, "The Global Food Crisis: ABCD of Food – How the Multinationals Dominate Trade," *The Guardian*, June 2, 2011, https://www.theguardian.com/global-development/poverty-matters/2011/jun/02/abcd-food-giants-dominate-trade.
[18] "Farming Opportunities," *National Sustainable Agriculture Coalition*, December 5, 2018, https://sustainableagriculture.net/our-work/issues/farming-opportunities/.
[19] National Young Farmers Coalition. "RELEASE: New census reveals threat to the future of agriculture as average age of farmers continues to rise." *Latest from Young Farmers*, 11 April 2019, https://www.youngfarmers.org/2019/04/census2017. Accessed 12 July 2023.

These barriers are further magnified for Black farmers, who face the compound challenges of both systemic racism and consolidation. In 1920, Black farmers made up 14 percent of the farmer population; in 2017 that figure fell to less than two percent.[20] Land consolidation cost Black communities more than $320 billion in wealth.[21]

Large agribusiness companies outsource and contract their farm work to individual farmers, but less competition means reduced negotiating power for farmers, resulting in farmers having little choice but to accept the lowest prices offered by the companies who wield significant market control. These low prices barely, if at all, cover a farmer's overhead costs. In 2022, the United States Department of Agriculture (USDA) found that the farmer's share of the food dollar reached a three decade record low of just 14.5 cents of every dollar spent.[22]

Consolidation also increases overhead costs for farmers, as a limited number of companies sell items that farmers depend on, such as tractors and the parts to replace them, and restricts innovation. Farmers are unable to pursue more sustainable and safer practices as a result of the constant need to produce vast quantities in a short period of time.

These are but a few examples of how agribusiness consolidation is creating financial harm for farmers, posing a market risk for the of the industry, and preventing small farmers from creating a robust, climate-friendly agricultural ecosystem.

Risk to Consumers

Consolidation in the food industry also poses a risk to consumers and their ability to feed their families. A 2019 study found that just four companies—Walmart, Kroeger, Costco, and Albertsons—accounted for 69 percent of all grocery sales in the country.[23] Of those, three are publicly-listed U.S. companies. Further, Kroeger announced its plans to purchase Albertsons in 2022.[24]

---

[20] "Bigger Farms, Bigger Problems," *Union of Concerned Scientists*, April 14, 2021. https://www.ucsusa.org/resources/bigger-farms-bigger-problems.

[21] Omanjana Goswami, "Farmland Consolidation, Not Chinese Ownership, Is the Real National Security Threat," *Union of Concerned Scientists*, March 2, 2023, https://blog.ucsusa.org/omanjana-goswami/farmland-consolidation-not-chinese-ownership-is-the-real-national-security-threat/.

[22] "Farm Share of U.S. Food Dollar Reached Historic Low in 2021," *USDA ERS*, November 28, 2022, https://www.ers.usda.gov/data-products/chart-gallery/gallery/chart-detail/?chartId=105281.

[23] "The Economic Cost of Food Monopolies: The Grocery Cartels," *Food and Water Watch*, November 2021, https://www.foodandwaterwatch.org/wp-content/uploads/2021/11/IB_2111_FoodMonoSeries1-SUPERMARKETS.pdf.

[24] "Kroger and Albertsons Companies Announce Definitive Merger Agreement," *The Kroger Co.*, October 14, 2022, https://ir.kroger.com/CorporateProfile/press-releases/press-release/2022/Kroger-and-Albertsons-Companies-Announce-Definitive-Merger-Agreement/default.aspx.

The same report found that from 1993 to 2019 the number of grocery stores declined by about 30 percent. The lack of competition gives consolidated grocery stores and food processors the power to raise food prices to increase their own profits, which in turn hurts the wallets of consumers, shippers, and farmers, and contributes to inflation.[25] For example, the National Farmers Union's "2023 Numbers of the Farmer's Share" found that the retail price for one pound of tomatoes to consumers was $2.00, while the farmer's share was a mere $0.42.[26]

Climate change will only exacerbate inflation risk to food prices[27] and poses a serious financial threat to consumers, particularly those who are food insecure.

Conclusion

Farmers and farm workers should not be used as political pawns by a hyper consolidated agribusiness industry actively fighting corporate disclosure requirements that they should already be responsible for reporting.

The climate crisis is already hurting the health and financial security of farmers, farm workers, and consumers. Yet some members of this committee continue to act as though climate change is risk free. What farmers, consumers, and farm workers need from policymakers are real solutions, not lip service. The solutions must be rooted in the fact that climate risk is a real threat that must be mitigated. Ultimately, our food and financial systems must become climate resilient and sustainable to support a healthy future for the nation.

We look forward to working with the committee on these issues and appreciate the opportunity to submit this letter for the record.

Sincerely,

Family Farm Defenders
Food & Water Watch
Institute for Agriculture and Trade Policy
Union of Concerned Scientists

---

[25] Drew DeSilver, "As Inflation Soars, a Look at What's inside the Consumer Price Index," *Pew Research Center*, January 24, 2022, https://www.pewresearch.org/short-reads/2022/01/24/as-inflation-soars-a-look-at-whats-inside-the-consumer-price-index/.

[26] "NFU Releases 2023 Farmer's Share of Fourth of July Food Dollar - National Farmers Union," *National Farmers Union*, June 30, 2023, https://nfu.org/2023/06/30/nfu-releases-2023-farmers-share-of-fourth-of-july-food-dollar/.

[27] Maximilian Kotz et al., "Working Paper Series: The Impact of Global Warming on Inflation: Averages, Seasonality and Extremes," *European Central Bank*, accessed July 15, 2023, https://www.ecb.europa.eu/pub/pdf/scpwps/ecb.wp2821~f008e5cb9e.en.pdf.

July 11, 2023

The Honorable Patrick McHenry
Chairman
House Financial Services Committee
2134 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Maxine Waters
Ranking Member
House Financial Services Committee
2221 Rayburn House Office Building
Washington, D.C. 20515

Chairman McHenry, Ranking Member Waters, and Members of the Committee,

We are writing to you as investor organizations that represent hundreds of investment firms and investment professionals that utilize sustainable investing in their portfolios. Sustainable investing and the incorporation of ESG criteria are already mainstream investing practice. As of year-end 2021, the US SIF Foundation identified $8.4 trillion in total US assets under management (AUM) using sustainable investing strategies. This represents 13 percent—or 1 in 8 dollars—of the total US assets under professional management. Both professional investors and everyday, hard-working Americans want to align their investments with critical ESG criteria to minimize long-term risks to their investments and maximize returns. A study by Morgan Stanley found that 85% of all investors are interested in incorporating sustainable investing strategies into their investment practices. Large corporations are seeing the value as well. According to IBM's annual CEO survey, "roughly 50% of CEOs and their executive teams now have compensation tied to sustainability goals, a significant jump from a year ago, when the figure was just 15%."

The U.S. economy has changed dramatically over the last 40 years. The value of a company used to be significantly derived from its tangible assets- inventory, factories, etc. Now, 90% of S&P 500 value is attributed to intangible assets- intellectual property, patents, and a company's workforce. Investors need to be able to respond to these shifts in our economy with complete, comprehensive data about the risks and opportunities faced by the companies they own. Sustainable investment has emerged as a market response to our evolving economy. It is an investment discipline that considers environmental, social, and governance (ESG) criteria, such as the current and future impacts of climate change, rising sea levels and heat waves, the treatment of workers and communities, and corporate governance issues. These additional data points, alongside traditional financial data, help understand long-term competitive financial risks and opportunities. Not all sustainable investment strategies are the same, nor is the field a monolith. Investors use all kinds of data and strategies to meet their financial objectives.

It's clear that investors are already integrating sustainable investment practices, but the landscape of ESG data makes it hard to measure companies across industries or across the market. The IBM 2023 CEO study found that "while 95% of companies have operational ESG goals, only 10% have made significant progress toward meeting them." According to the CEOs interviewed for the study, "tracking and measurement in the sustainability space is a huge issue." Investors require the ability to understand the full picture of a company's risks, opportunities and efforts to

address these areas for the future. There is still significant work that needs to be done for disclosed information from businesses to reach the level of investor needs.

There can be real financial costs if ESG-related risks are not well managed. For example, the recent Norfolk Southern train derailment raised numerous concerns associated with the company's management and practices that may be considered ESG issues and affect investors. Following the derailment, Norfolk Southern's stock price dropped 10 percent- indicating that a lack of oversight of these issues has real consequences for shareholder value. The economic impact of climate change is another risk investors need to fully understand. Climate change was the number one ESG issue for both asset managers and institutional investors in the US SIF Foundation's 2022 Trends Report and has been one of the top issues for investors for more than a decade. The National Oceanic and Atmospheric Administration showed that in 2022 there was $165 billion in damages due to climate change-fueled extreme weather, including 18 different weather disasters that each cost a billion dollars or more. As governments move to keep temperatures under the critical 1.5 degrees Celsius threshold, companies need to disclose to their shareholders how this move to a decarbonized economy will affect their business.

The Securities and Exchange Commission (SEC) has the ability and the mandate to require standardized disclosures from companies that would help investors better price the risks and opportunities presented by a warming climate or the health and safety of the U.S. workforce. In their January 2023 comment letter about the proposed climate risk disclosure rule, securities law experts reiterated the SEC's distinct mandate to require increased disclosure, saying, "Congress structured securities regulation as principally disclosure-based, instructing the SEC to regulate the capital markets through an extensive disclosure regime for publicly traded companies. The SEC's statutory authority over disclosure is broad by congressional design, extending not just to information relevant to investor trading decisions but also to information used by investors in connection with the exercise of their voting rights."

Investors have shown support for both more information about corporations' long-term risks and opportunities and for the SEC to standardize disclosures. At the beginning of the 2023 proxy season, investors filed 542 shareholder resolutions that raised important issues with company management about ESG risks. Shareholder engagement is a critical tool for investors to raise important issues with management, other shareholders, the board, and the public. Moreover, resolutions need not come to a vote to be effective. Productive discussions between management and shareholders often resolve issues of concern before a shareholder proposal is ever filed. At the SEC, investors have submitted comments overwhelmingly in favor of more disclosure of data around long-term risks generally, as well as data related specifically to climate risks.

Investors have choices in the market. While they are not forced to invest in ESG-related funds, the market reflects the reality that accounting for long-term risks and opportunities is just good business. We hope that the Committee will consider the evidence we've laid out here and the alignment on responsible investment by retail and institutional investors alike and we appreciate your attention to this important issue.

Sincerely,

Ceres

Interfaith Center on Corporate Responsibility

U.S. Impact Investing Alliance

US SIF: The Sustainable Investment Forum

Cc: Members of the House Financial Services Committee

July 11, 2023

The Honorable Patrick McHenry
Chairman
House Committee on Financial Services
2129 Rayburn HOB Washington, DC 20515

The Honorable Maxine Waters
Ranking Member
House Committee on Financial Services
4340 O'Neill HOB
Washington, DC 20515

House Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

Re: Upcoming ESG Hearings and Markup

Dear Chairman McHenry, Ranking Member Waters, and other members of the House Committee on Financial Services:

We, the undersigned organizations, write to you today to express our opposition to the policy agenda apparent from a recent ESG Working Group memorandum[1] and a series of bills introduced in the House.[2] That policy agenda seeks to: 1) insulate the management of public companies from investor input and accountability; and 2) undermine regulations that would equip investors with more information to make better decisions about their investments.

We oppose insulating the management of public companies from investor input and accountability.

Workers saving for retirement are long-term investors who hold equity in a broad swath of public companies for decades. As Illinois State Treasurer Michael Frerichs repeatedly noted in a recent

[1] ESG Working Group, House Committee on Financial Services, "MEMORANDUM: Preliminary Report on ESG Climate Related Financial Services Concerns," Jun. 23, 2023, *available at* https://financialservices.house.gov/uploadedfiles/hfsc_esg_working_group_memo_final.pdf.
[2] H.R. 448, Putting Investors First Act of 2023, *available at* https://www.congress.gov/bill/118th-congress/house-bill/448; H.R. 8521, INDEX Act, *available at* https://www.congress.gov/bill/117th-congress/house-bill/8521; H.R. 7151, Ensuring Sound Guidance Act, *available at* https://www.congress.gov/bill/117th-congress/house-bill/7151/text?s=1&r=90; H.R. 9408, Mandatory Materiality Requirement Act of 2022, *available at* https://www.congress.gov/bill/117th-congress/house-bill/9408; H.R.1018, Protect Farmers from the SEC Act, *available at* https://www.congress.gov/bill/118th-congress/house-bill/1018; H.R.3057, Scope 3 Act, *available at* https://www.congress.gov/bill/118th-congress/house-bill/3057/text.

House Oversight Committee hearing, these investors are interested in how a company performs over the next quarter century, not the next quarter.[3] Because their retirement security depends on the ability of the many public companies they are invested in to engage in long-term, sustainable value creation, workers are incentivized to use the tools at their disposal to push companies toward this goal and away from short-term, risky value extraction that jeopardizes the long-term value of their investments. These tools include engaging with companies, filing shareholder proposals, and voting their shares in line with their interests. With these tools, shareholders can push companies to address issues affecting their long-term investments, including those related to workplace safety, human capital, racial equity, environmental sustainability, and workers' freedom of association.

Unfortunately, the policy agenda outlined by the majority in the ESG Working Group memorandum and in the bills they have introduced demonstrates a desire to shut off investors' access to these tools and insulate management from investor input and accountability by targeting various actors in the corporate governance ecosystem:

- Perceiving **proxy advisory firms** to be too unfriendly to management, the majority wants to interfere with these firms' ability to give sound voting advice to their clients by making it more costly and risky to advise voting against management's wishes.[4]
- The majority wants to make it more difficult for shareholders to file **shareholder proposals** and to have those proposals considered by the rest of the shareholders.[5]
- The majority wants to both make it easier for **asset managers** to eschew their responsibility to vote proxies in the best interest of their clients and make it harder for them to vote against management's wishes.[6]
- The majority wants to muddy the legal waters that determine how investment advisors and those managing workers' retirement savings under ERISA can make investment decisions[7] — including proxy voting and engagement decisions — by introducing an

[3] House Committee on Oversight and Accountability, "ESG Part I: An Examination of Environmental, Social, and Governance Practices with Attorneys General," May 10, 2023, *available at* https://oversight.house.gov/hearing/esg-part-i-an-examination-of-environmental-social-and-governance-practices-with-attorneys-general/.

[4] H.R. 448, Putting Investors First Act of 2023, sections 3 & 8, *available at* https://www.congress.gov/bill/118th-congress/house-bill/448; ESG Working Group, House Committee on Financial Services, "MEMORANDUM: Preliminary Report on ESG Climate Related Financial Services Concerns," 2-7, Jun. 23, 2023, *available at* https://financialservices.house.gov/uploadedfiles/hfsc_esg_working_group_memo_final.pdf.

[5] H.R. 448, Putting Investors First Act of 2023, section 6, *available at* https://www.congress.gov/bill/118th-congress/house-bill/448.

[6] HR 448, Putting Investors First Act of 2023, section 4, *available at* https://www.congress.gov/bill/118th-congress/house-bill/448; H.R.8521, INDEX Act, *available at* https://www.congress.gov/bill/117th-congress/house-bill/8521.

[7] U.S. Congressman Barr, "Barr and Allen Introduce ESG Act to Protect Investors and Preserve Access to Capital for Energy Producers," Jun. 21, 2023, *available at* https://barr.house.gov/press-releases?ID=9DB5373C-A4BF-4964-8283-6B186252CDE7; H.R.7151, Ensuring Sound Guidance Act, *available at* https://www.congress.gov/bill/117th-congress/house-bill/7151/text?s=1&r=90.

unworkable distinction between so-called pecuniary and non-pecuniary factors.[8]

We oppose undermining regulations that would equip investors with more information to make better decisions about their investments.

Investor protection is a central part of the mission of the Securities and Exchange Commission (SEC). At a time when it is undeniable that climate risk is a significant financial risk,[9] the SEC proposed an important rule that will bring much-needed transparency to investors about how public companies are contending with climate risk and capturing emissions reduction opportunities created by new laws like the Inflation Reduction Act. Investors nearly universally support the rule's main provisions,[10] and securities law experts agree that the proposal is clearly within agency authority.[11] Additionally, the SEC is expected to propose a rule on human capital management disclosures to provide investors with visibility into how public companies manage their workforce, a central component of long-term value creation. These two rules aim to give investors access to consistent, comparable, and decision-useful data that would help them and asset managers get a fuller picture of risks and opportunities to make investment decisions and for the valuation of securities.

Unfortunately, the ESG Working Group memorandum expresses strong opposition to these two rules,[12] and members of the majority have introduced three bills that would take direct aim at the SEC's investor protection mission:

- The **Mandatory Materiality Requirement Act** would stymie the SEC's ability to fulfill its investor protection mission by making it harder for the agency to issue effective rules requiring disclosures that are important to investors.[13]
- The **Protect Farmers from the SEC Act** would block the SEC's ability to require information from public companies that is critical for investors to protect themselves

[8] David J. Berger, David H. Webber, & Beth Young, "The Liability Trap: Why the ALEC Anti-ESG Bills Create a Legal Quagmire for Fiduciaries Connected with Public Pensions," Feb. 15, 2023, *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4360119.
[9] *See generally* Financial Stability Oversight Council, "Report on Climate-Related Financial Risk," 2021, *available at* https://home.treasury.gov/system/files/261/FSOC-Climate-Report.pdf.
[10] Steven M. Rothstein, "Analysis shows that investors strongly support the SEC's proposed climate disclosure rule," Ceres, Oct. 11, 2022, *available at* https://www.ceres.org/news-center/blog/analysis-shows-investors-strongly-support-secs-proposed-climate-disclosure-rule.
[11] Jill E. Fisch, George S. Georgiev, Donna M. Nagy, & Cynthia A. Williams, "Climate Change, West Virginia v. EPA, and the SEC's Distinctive Statutory Mandate," Summer 2022, *available at* https://www.sec.gov/comments/s7-10-22/s71022-20154853-323117.pdf.
[12] ESG Working Group, House Committee on Financial Services, "MEMORANDUM: Preliminary Report on ESG Climate Related Financial Services Concerns," 13-14, Jun. 23, 2023, *available at* https://financialservices.house.gov/uploadedfiles/hfsc_esg_working_group_memo_final.pdf.
[13] H.R.9408, Mandatory Materiality Requirement Act of 2022, *available at* https://www.congress.gov/bill/117th-congress/house-bill/9408.

from climate-related risks.[14] The SEC climate disclosure rule, as proposed, includes extensive protections to avoid burdens on small private businesses — including small farmers. The Institute for Agriculture and Trade Policy puts it bluntly: "Agribusinesses are wrongly fighting the wrong battle by enlisting farmers and ranchers to falsely claim that the SEC climate disclosure rule applies to them."[15] Organizations that represent the interests of small farmers wrote the SEC in March 2023 in support of finalizing the rule inclusive of Scope 1, 2, and 3 emissions.[16]

- The **Scope 3 Act** would block the SEC from requiring Scope 3 emissions from any issuer.[17] Scopes 3 emissions disclosure has nearly unanimous support from investors[18] who told the SEC during the comment period that they need this information to assess transition risk of companies.

Behind this policy agenda that threatens investor protection and corporate accountability is the fossil fuel industry, bankrolling efforts to protect their own short-term interests regardless of what it means for workers' retirement security, our financial system, and beyond.[19] Unfortunately, this effort often involves the use of anti-woke rhetoric. Although woke simply means to be aware of racial and social injustices, some are using anti-woke rhetoric to fuel racial resentment in pursuit of policies that serve short-term corporate interests at the expense of working people, their retirement security, and corporate accountability.

We urge you to forcefully take a stand against these policies and this approach. For further discussion, contact Natalia Renta at natalia@ourfinancialsecurity.org.

Sincerely,

National & international organizations

Americans for Financial Reform
American Federation of Labor and Congress of Industrial Organizations (AFL-CIO)
American Federation of Teachers (AFT)

---

[14] H.R.1018 - Protect Farmers from the SEC Act, *available at* https://www.congress.gov/bill/118th-congress/house-bill/1018.
[15] Steve Suppan, "Agribusiness opposition to the proposed SEC climate-related financial disclosure rule," Institute for Agriculture & Trade Policy, Aug. 12, 2022, *available at* https://www.iatp.org/agribusiness-opposition-proposed-sec-rule.
[16] Group letter to the Securities & Exchange Commission on climate-risk disclosure proposed rule, *available at* https://www.sec.gov/comments/s7-10-22/s71022-20159767-327935.pdf.
[17] H.R.3057, Scope 3 Act, *available at* https://www.congress.gov/bill/118th-congress/house-bill/3057/text.
[18] Steven M. Rothstein, "Analysis shows that investors strongly support the SEC's proposed climate disclosure rule," Ceres, Oct. 11, 2022, *available at* https://www.ceres.org/news-center/blog/analysis-shows-investors-strongly-support-secs-proposed-climate-disclosure-rule.
[19] Jessica Church, "The Big Money Behind the Fight to Ban Responsible Investing," Inequality.org, Jul. 3, 2023, *available at* https://inequality.org/research/big-money-behind-fight-to-ban-responsible-investing/.

As You Sow
Businesses for a Livable Climate
CatholicNetwork US
Center for LGBTQ Economic Advancement & Research (CLEAR)
Change Finance, PBC
Climate Finance Action
Climate Hawks Vote
Communications Workers of America (CWA)
Environmental Defense Fund
Green America
Honor the Earth
Interfaith Center on Corporate Responsibility
Maryknoll Sisters
Public Citizen
RapidShift Network
Rhia Ventures
Rise Economy
Save EPA
Service Employees International Union (SEIU)
Seventh Generation Interfaith Coalition for Responsible Investment
Sierra Club
Small Business Alliance
SOC Investment Group
Stance Capital, LLC
System Change Not Climate Change
The Horizon Project
Take on Wall Street
Trillium Asset Management
Tulipshare
Union of Concerned Scientists
Unitarian Universalist Association
US Partnership for Education for Sustainable Development
Women's Earth and Climate Action Network (WECAN)
Zevin Asset Management

State & local organizations

Accelerate Neighborhood Climate Action
Call to Action Colorado
CO Businesses for a Livable Climate

Community for Sustainable Energy
Greater New Orleans Housing Alliance
I-70 Citizens Advisory Group
Indivisible Ambassadors
Larimer Alliance for Health, Safety and Environment
Littleton Business Alliance
Mayfair Park Neighborhood Association Board
Mental Health & Inclusion Ministries
The Mind's Eye
Montbello Neighborhood Improvement Association
Southwest Organization for Sustainability
Spirit of the Sun, Inc.
The Green House Connection Center
Unite North Metro Denver
Wall of Women
Western Slope Businesses for a Livable Climate
Womxn from the Mountain
Working for Racial Equity

Mr. Jonathan Berry

1. Which of the following options best describes your self-identified race? (you may choose more than one)
    a. White or Caucasian
    b. Black or African American
    c. Hispanic/Latinx
    d. Asian e. Middle Eastern/North African
    f. Choose not to answer
    g. Prefer to self-describe (please specify)

2. Which of the following options best describes your gender identity?
    a. Woman
    b. Man
    c. Non-binary
    d. Transgender Man
    e. Transgender Woman
    f. Choose not to answer
    g. Prefer to self-describe (please specify)

Answer of Jonathan Berry: These questions are inappropriate and I decline to answer.

Bipartisan Policy Center
Where democracy gets to work.

Questions for the Record For

Timothy M. Doyle
Senior Policy Advisor
Bipartisan Policy Center

Before the: U.S. House of Representatives
Committee on Financial Services
Subcommittee on Capital Markets

Hearing on: "Reforming the Proxy Process to Safeguard Investor Interests"

Date: July 13, 2023

Questions for the record from Ranking Member Maxine Waters

1. *Which of the following options best describes your self-identified race? (You may choose more than one)*
    a. *White or Caucasian*
    b. *Black or African American*
    c. *Hispanic/Latinx*
    d. *Asian*
    e. *Middle Eastern/North African*
    f. *Chose not to answer*

White or Caucasian

2. *Which of the following options best describes your gender identity?*
    a. *Woman*
    b. *Man*
    c. *Non-binary*
    d. *Transgender man*
    e. *Transgender woman*
    f. *Choose not to answer*
    g. *prefer to self-describe (please specify)*

Man

Questions for the Record from Ranking Member Maxine Waters
Subcommittee Hearing, entitled "Reforming the Proxy Process to Safeguard Investor Interests."
July 13, 2023 10am

a. Ms. Nell Minow

1. Which of the following options best describes your self-identified race? (you may choose more than one)

   a. White or Caucasian
   a. Black or African American
   b. Hispanic/Latinx
   c. Asian
   d. Middle Eastern/North African
   e. Choose not to answer
   f. Prefer to self-describe (please specify)

2. Which of the following options best describes your gender identity?
   a. Woman
   b. Man
   c. Non-binary
   d. Transgender Man
   e. Transgender Woman
   f. Choose not to answer
   g. Prefer to self-describe (please specify)

Questions for the Record for

Chris Netram
Managing Vice President, Policy
National Association of Manufacturers

Before the

U.S. House of Representatives
Committee on Financial Services
Subcommittee on Capital Markets

Hearing on

"Reforming the Proxy Process to Safeguard Investor Interests"

July 13, 2023

Questions for the Record from Ranking Member Maxine Waters

1. *Which of the following options best describes your self-identified race? (you may choose more than one)*
    a. *White or Caucasian*
    b. *Black or African American*
    c. *Hispanic/Latinx*
    d. *Asian*
    e. *Middle Eastern/North African*
    f. *Choose not to answer*

Asian

2. *Which of the following options best describes your gender identity?*
    a. *Woman*
    b. *Man*
    c. *Non-binary*
    d. *Transgender Man*
    e. *Transgender Woman*
    f. *Choose not to answer*
    g. *Prefer to self-describe (please specify)*

Man

VANDERBILT UNIVERSITY
Owen Graduate School of Management

Dr. Joshua T. White
Assistant Professor of Finance
Brownlee O. Curry, Jr. Dean's Faculty Fellow

July 21, 2023

Re: Questions for the Record (QFR)

Dear Chair Waters:

It was my privilege to testify before the Subcommittee on Capital Markets, under the House Financial Services Committee, on July 13, 2023. The hearing was entitled: "Reforming the Proxy Process to Safeguard Investor Interests."

I appreciate your request for additional information regarding my demographic information. For your records, my responses are below in bold. I identify as a white man.

1. Which of the following options best describes your self-identified race? (you may choose more than one)
    a. **White or Caucasian**
    b. Black or African American
    c. Hispanic/Latinx
    d. Asian
    e. Middle Eastern/North African
    f. Choose not to answer
    g. Prefer to self-describe (please specify)

2. Which of the following options best describes your gender identity?
    a. Woman
    b. Man
    c. Non-binary
    d. Transgender Man
    e. Transgender Woman
    f. Choose not to answer
    g. Prefer to self-describe (please specify)

With kind regards,

Joshua T. White, Ph.D.

401 21st Ave. S
Office 358
Nashville, TN 37203
E josh.white@vanderbilt.edu
W https://www.joshua-t-white.com/