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SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 271 and 276

[Release Nos. IA-5325; IC-33605]

Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers

AGENCY: Securities and Exchange Commission.

ACTION: Guidance.

SUMMARY: The Securities and Exchange Commission (the “SEC” or the “Commission”) is publishing guidance regarding the proxy voting responsibilities of investment advisers under its regulations issued under the Investment Advisers Act of 1940 (the “Advisers Act”), and Form N-1A, Form N-2, Form N-3, and Form N-CSR under the Investment Company Act of 1940 (the “Investment Company Act”).

DATES: *Effective:* [INSERT DATE OF PUBLICATION IN THE FEDERAL REGISTER].

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SUPPLEMENTARY INFORMATION: The Commission is publishing guidance regarding the proxy voting responsibilities of investment advisers under 17 CFR 275.206(4)-6 [Rule 206(4)-6 under the Advisers Act [15 U.S.C. 80b]],¹ Form N-1A,² Form N-2,³ Form N-3,⁴ and

¹ Unless otherwise noted, when we refer to the Advisers Act, or any paragraph of the Advisers Act, we are referring to 15 U.S.C. 80b of the United States Code, at which the Advisers Act is codified, and when we refer to rules under the Advisers Act, or any paragraph of these rules, we are referring to title 17, part 275 of the Code of Federal Regulations [17 CFR part 275], in which these rules are published.

² Referenced in 17 CFR 274.11A.

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I. INTRODUCTION

Investment advisers regularly are faced with an array of decisions regarding voting of equity securities on behalf of their clients, whether those clients are individual investors, funds or other institutional investors.⁷ In various contexts, and in respect of a wide range of matters submitted to shareholders for a vote, investment advisers that have agreed to take on proxy voting authority are called upon to make voting determinations.

³ Referenced in 17 CFR 274.11a-1.

⁴ Referenced in 17 CFR 274.11b.

⁵ Referenced in 17 CFR 274.128.

⁶ Unless otherwise noted, when we refer to the Investment Company Act, or any paragraph of the Investment Company Act, we are referring to 15 U.S.C. 80a of the United States Code, at which the Investment Company Act is codified, and when we refer to rules under the Investment Company Act, or any paragraph of these rules, we are referring to title 17, part 270 of the Code of Federal Regulations [17 CFR part 270], in which these rules are published.

⁷ Investment advisers owe each of their clients a fiduciary duty under the Advisers Act, which “must be viewed in the context of the agreed-upon scope of the relationship between the adviser and the client.” Commission Interpretation Regarding Standard of Conduct for Investment Advisers, Release No. IA-5248 (June 5, 2019), 84 FR 33669, at 33671 (July 12, 2019) (“Fiduciary Interpretation”). In the case of a registered investment company (“fund”), the scope of this relationship is defined by the advisory agreement between the investment adviser and its client (*i.e.*, the fund), and the fund board has the authority to set the scope of voting authority in accordance with its fiduciary duty. With respect to funds, the Investment Company Institute noted that a fund board typically delegates its proxy voting duties to the fund’s investment adviser. During the 2017 proxy season, funds cast more than 7.6 million votes for proxy proposals, and the average fund voted on 1,504 separate proxy proposals for U.S. listed portfolio companies (figures exclude companies domiciled outside the United States.). See Letter dated Mar. 15, 2019 from Paul Schott Stevens, President and CEO, Investment Company Institute (“ICI Letter II”) at p. 3. Unless otherwise noted, letters cited herein were submitted in response to the Statement Announcing SEC Staff Roundtable on the Proxy Process, July 30, 2018 available at <https://www.sec.gov/comments/4-725/4-725.htm>.

In general, matters are put forth for a shareholder vote either by the issuer⁸ or by a shareholder or group of shareholders. The submission of matters for a vote by shareholders typically occurs in connection with a meeting of shareholders, including annual shareholder meetings and special shareholder meetings.⁹ Some matters appear regularly and consistently at each annual meeting of shareholders, such as the shareholder vote on whether to ratify the issuer's selection of an outside auditor.¹⁰ Other matters, such as shareholder votes on proposed mergers, acquisitions, or other corporate actions and matters proposed by a shareholder or group of shareholders, are generally more idiosyncratic in substance and timing.

Investment advisers are fiduciaries that owe each of their clients duties of care and loyalty with respect to services undertaken on the client's behalf, including voting.¹¹ In the context of voting, the specific obligations that flow from the investment adviser's fiduciary duty depend upon the scope of voting authority assumed by the adviser.¹² To satisfy its fiduciary duty in making any voting determination, the investment adviser must make the determination in the best interest of the client and must not place the investment adviser's own interests ahead of the interests of the client.

⁸ As used in this Release, the terms "company" and "issuer" refer to the issuer of the securities for which proxies are solicited.

⁹ Concept Release on the U.S. Proxy System, Release No. 34-62495 (July 14, 2010), 75 FR 42982 (July 22, 2010) ("Concept Release").

¹⁰ Many of these matters are required to be submitted to shareholders as a result of federal law, state law, exchange requirements or the company's governance documents. *See, e.g.*, Section 14A(a) of the Securities Exchange Act of 1934 ("say-on-pay" votes); 8 Del. C. 1953, sec. 211 (annual meeting to elect directors); NYSE Listed Company Manual Section 312.03(b) (shareholder approval for certain related party transactions involving issuances of common stock); and NASDAQ Rule 5635(a) (shareholder approval is required in certain instances prior to the issuance of securities in connection with the acquisition of the stock or assets of another company).

¹¹ *See* Fiduciary Interpretation, 84 FR 33669, at n. 32.

¹² *See* Fiduciary Interpretation, 84 FR 33669, at 33671–72.

Specifically, an investment adviser's duty of care includes, among other things, the duty to provide advice that is in the best interest of the client.¹³ Where an investment adviser has assumed the authority to vote on behalf of its client, the investment adviser, among other things, must have a reasonable understanding of the client's objectives and must make voting determinations that are in the best interest of the client.¹⁴ As discussed below, for an investment adviser to form a reasonable belief that its voting determinations are in the best interest of the client, it should conduct an investigation reasonably designed to ensure that the voting determination is not based on materially inaccurate or incomplete information.¹⁵ Further, Rule 206(4)-6 under the Advisers Act provides that it is a fraudulent, deceptive, or manipulative act, practice, or course of business for an investment adviser registered or required to be registered with the Commission to exercise voting authority with respect to client securities unless the adviser, among other things, adopts and implements written policies and procedures that are reasonably designed to ensure that the investment adviser votes proxies in the best interest of its clients.¹⁶ We discuss further below how the fiduciary duty and Rule 206(4)-6 relate to an investment adviser's exercise of voting authority on behalf of clients.

¹³ See Fiduciary Interpretation, 84 FR 33669, at 33672.

¹⁴ See Fiduciary Interpretation, 84 FR 33669, at 33673 (discussing an adviser's obligation to make a reasonable inquiry into its client's financial situation, level of financial sophistication, investment experience and financial goals and have a reasonable belief that the advice it provides is in the best interest of the client based on the client's objectives).

¹⁵ See Fiduciary Interpretation, 84 FR 33669, at 33674. See also Proxy Voting by Investment Advisers, Release No. IA-2106 (Jan. 31, 2003), 68 FR 6585 (Feb. 7, 2003) ("Proxy Voting Release"), at 6586 (explaining that an adviser's duty of care with respect to proxy voting requires, among other things, an adviser with proxy voting authority to monitor corporate events.)

¹⁶ See Rule 206(4)-6 under the Advisers Act. With respect to conflicts of interests, the Commission brought a settled enforcement action against an investment adviser that had voting authority, where the adviser's policies and procedures did not include how the adviser would address potential conflicts that may arise between its interests and those of its clients. See *In the Matter of Intech Investment Management, LLC and David E. Hurley*, Release No. IA-2872 (May 7, 2009).

When making voting determinations on behalf of clients, many investment advisers retain proxy advisory firms to perform a variety of functions and services. Some of these are administrative, such as providing the investment adviser with an electronic platform that enables the adviser to manage voting mechanics more efficiently. Other services provided by proxy advisory firms relate to the substance of voting, such as: providing research and analysis regarding the matters subject to a vote; promulgating general voting guidelines that investment advisers can adopt; and making voting recommendations to investment advisers on specific matters subject to a vote.¹⁷ We understand that these voting recommendations may be based on a proxy advisory firm's own voting guidelines or on custom voting guidelines that the investment adviser has created.¹⁸ We understand further that custom guidelines, where they are used, may be more or less detailed, depending on the level of instruction an investment adviser has provided to a proxy advisory firm.¹⁹ Contracting with proxy advisory firms to provide these types of functions and services can reduce burdens for investment advisers (and potentially reduce costs for their clients) as compared to conducting them in-house.

We understand further that an investment adviser that has assumed the authority to vote proxies on behalf of its clients may look to the voting recommendations of a proxy advisory firm when the investment adviser has a conflict of interest, such as if, for example, the investment

¹⁷ See, e.g., Letter dated Dec. 31, 2018 from Gail C. Bernstein, General Counsel, Investment Adviser Association ("IAA Letter"), at p. 2; ICI Letter II, at pp. 8-9; Letter dated Jan. 16, 2019 from Dieter Waizenegger, Executive Director, CtW Investment Group at p. 2 (explaining that the value-added analysis provided by proxy advisory firms is especially important during the U.S. proxy season); see generally Roundtable on the Proxy Process, Transcript (Nov. 15, 2018) available at <https://www.sec.gov/files/proxy-round-table-transcript-111518.pdf>.

¹⁸ See, e.g., IAA Letter, at 2; Letter dated Nov. 14, 2018 from Paul Schott Stevens, President and CEO, Investment Company Institute ("ICI Letter I"), at p. 34.

¹⁹ See, e.g., Letter dated Nov. 14, 2018 from Katherine Rabin, Chief Executive Officer, Glass Lewis, at p. 2 (noting that institutional investors who engage a proxy advisory firm are opting for such firms to execute increasingly detailed policies).

adviser's interests in an issuer or voting matter differ from those of some or all of its clients.

While this third-party input into such an investment adviser's voting decision may mitigate the investment adviser's potential conflict of interest, it does not relieve that investment adviser of (1) its obligation to make voting determinations in the client's best interest, or (2) its obligation to provide full and fair disclosure of the conflicts of interest and obtain informed consent from its clients.²⁰

We have solicited feedback on, and our staff has previously provided guidance regarding, various means investment advisers can use to fulfill their proxy voting responsibilities, including the retention and use of proxy advisory firms. In addition, we and our staff have engaged with the public through various forums and statements on a variety of issues related to the proxy voting process, including those discussed below.

For example, in 2010, the Commission issued a concept release that sought public comment about, among other things, the role and legal status of proxy advisory firms within the U.S. proxy system.²¹ In 2013, the staff held a roundtable on the use of proxy advisory firm services by institutional investors and investment advisers.²² In 2014, the staff of the Divisions of Investment Management and Corporation Finance issued a Staff Legal Bulletin ("SLB 20") to provide (1) the staff's views regarding an investment adviser's responsibilities in voting client proxies and retaining proxy advisory firms, as well as (2) guidance about the availability and

²⁰ See Fiduciary Interpretation, 84 FR 33669, at 33675-76 ("To meet its duty of loyalty, an adviser must make full and fair disclosure to its clients of all material facts relating to the advisory relationship.... In addition, an adviser must eliminate or at least expose through full and fair disclosure all conflicts of interest which might incline an investment adviser—consciously or unconsciously—to render advice which was not disinterested.") (internal citations omitted).

²¹ See Concept Release, 75 FR 42982. The comment letters received in response to the Concept Release are available at <https://www.sec.gov/comments/s7-14-10/s71410.shtml>.

²² See SEC Announces Agenda, Panelists for Roundtable on Proxy Advisory Services (Nov. 27, 2013), available at <https://www.sec.gov/news/press-release/2013-253>. The letters received in response to the announcement are available at <https://www.sec.gov/comments/4-670/4-670.shtml>.

requirements of two exemptions to the federal proxy rules that are often relied upon by proxy advisory firms.²³ The SEC’s Office of Compliance Inspections and Examinations has also examined investment advisers’ compliance with their fiduciary duty when voting proxies on behalf of investors, including review of risk areas related to conflicts of interest, proxy voting policies and procedures, and oversight of proxy advisory firms, among other issues.²⁴ Most recently, the staff hosted a roundtable on the proxy process in November 2018 (the “2018 Roundtable”) that included a panel on the role of proxy advisory firms and their use by investment advisers.²⁵ In connection with the 2018 Roundtable, the public was invited to provide input on questions that arise regarding the use of proxy advisory firms and their activities.²⁶ We have carefully considered the feedback received on these topics, and with the benefit of this extensive body of information, historical experience, and engagement, the Commission is today issuing guidance to investment advisers about their voting responsibilities.²⁷

²³ See SEC Staff Legal Bulletin No. 20, Proxy Voting: Proxy Voting Responsibilities of Investment Advisers and Availability of Exemptions from the Proxy Rules for Proxy Advisory Firms (June 30, 2014), available at <https://www.sec.gov/interps/legal/cfslb20.htm>. SLB 20 represents the views of the staff of the Divisions of Investment Management and Corporation Finance. It is not a rule, regulation, or statement of the Commission. Furthermore, the Commission has neither approved nor disapproved its content. SLB 20, like all staff guidance, has no legal force or effect: it does not alter or amend applicable law, and it creates no new or additional obligations for any person.

²⁴ See, e.g., SEC, Office of Compliance Inspections and Examinations, 2015 Examination Priorities for 2015, available at <https://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2015.pdf>.

²⁵ See Chairman Jay Clayton, Statement Announcing SEC Staff Roundtable on the Proxy Process, available at <https://www.sec.gov/news/public-statement/statement-announcing-sec-staff-roundtable-proxy-process>.

²⁶ See Comments on Statement Announcing SEC Staff Roundtable on the Proxy Process; File No. 4-725, available at <https://www.sec.gov/comments/4-725/4-725.htm>.

²⁷ The Commission today is also issuing interpretation and guidance regarding certain rules promulgated under Section 14 of the Securities Exchange Act of 1934 regarding proxy voting advice. Release No. 34 – 86721 (August 21, 2019), published elsewhere in this issue of the Federal Register.

In Section II below, we discuss how the fiduciary duty and Rule 206(4)-6 relate to an investment adviser's exercise of voting authority on behalf of clients. In that Section, we are focused in particular on providing guidance to investment advisers that retain a proxy advisory firm to assist them in some aspect of their proxy voting responsibilities.²⁸ More specifically, we have followed the question and answer format used by the staff in SLB 20 as we understand that many investment advisers have found that format useful.

In this guidance, we provide examples to help facilitate investment advisers' compliance with their proxy voting responsibilities; however, these examples are not the only way by which investment advisers could comply with their principles-based fiduciary duty imposed on them by the Advisers Act.

We encourage investment advisers and proxy advisory firms to review their policies and practices in light of the guidance below in advance of next year's proxy season. To the extent that firms identify operational or other questions in the course of that review, we encourage them to contact the staff of the Division of Investment Management.

The Commission will consider any questions or other feedback on its guidance regarding the proxy voting responsibilities of investment advisers under their fiduciary duty and Rule 206(4)-6 under the Advisers Act, and Form N-1A, Form N-2, Form N-3, and Form N-CSR under the Investment Company Act to evaluate whether additional guidance might be appropriate in the future. Based on any feedback received, the Commission could supplement this guidance.

²⁸ The staff previously provided its views on certain of these questions in SLB 20.

II. GUIDANCE REGARDING INVESTMENT ADVISERS' PROXY VOTING RESPONSIBILITIES AND DISCLOSURES ON FORM N-1A, FORM N-2, FORM N-3, AND FORM N-CSR

Question 1: How may an investment adviser and its client, in establishing their relationship, agree upon the scope of the investment adviser's authority and responsibilities to vote proxies on behalf of that client?

Response: As we recently stated, "[t]he fiduciary duty follows the contours of the relationship between the adviser and its client, and the adviser and its client may shape that relationship by agreement, provided that there is full and fair disclosure and informed consent."²⁹ Accordingly, an investment adviser is not required to accept the authority to vote client securities, regardless of whether the client undertakes to vote the proxies itself.³⁰ If an investment adviser does accept voting authority, it may agree with its client, subject to full and fair disclosure and informed consent, on the scope of voting arrangements, including the types of matters for which it will exercise proxy voting authority. While the application of the investment adviser's fiduciary duty in the context of proxy voting will vary with the scope of the voting authority assumed by the investment adviser, the relationship in all cases remains that of a fiduciary to the client.³¹

Differences in agreements between investment advisers and their clients as to the scope of the advisory relationship may result in a variety of arrangements for voting client securities.

²⁹ See *Fiduciary Interpretation*, 84 FR at 33677, footnotes 67-70 and accompanying text for a detailed discussion of informed consent and how it is generally considered on an objective basis and may be inferred. See also Form ADV, Part 2A, Item 17, and Proxy Voting Release, 68 FR 6585, at n. 19.

³⁰ We believe, however, that to the extent an investment adviser has discretionary authority to manage the client's portfolio and has not agreed with the client to a narrower scope of voting authority through full and fair disclosure and informed consent, the adviser's responsibility for making voting determinations is implied. See Proxy Voting Release, 68 FR 6585 at n. 10.

³¹ As we recently stated, "an adviser's federal fiduciary duty may not be waived, though it will apply in a manner that reflects the agreed-upon scope of the relationship." See *Fiduciary Interpretation*, 84 FR 33669, at 33672.

While a client and its investment adviser may agree that the client will delegate all of its proxy voting authority to its investment adviser, the client and the investment adviser may instead agree (in the manner described above) to other proxy voting arrangements in which the investment adviser would not assume all of the proxy voting authority, or in which the investment adviser would only assume the authority to vote on behalf of the client in limited circumstances or not at all.³² Following are several non-exhaustive examples of possible voting arrangements to which a client and its investment adviser may agree, subject to full and fair disclosure and informed consent:³³

- A client and its investment adviser may agree that the investment adviser should exercise voting authority pursuant to specific parameters designed to serve the client’s best interest. For example, the client and the investment adviser may agree that, absent receipt of a contrary instruction from the client or a determination by the investment adviser that voting a particular proposal in a different way would be in the client’s best interest (*e.g.*, if voting differently would further the investment strategy being pursued by the investment adviser on behalf of the client):
 - The investment adviser will vote in accordance with the voting recommendations of management of the issuer. Such an arrangement could be subject to conditions, for example additional analysis by the investment adviser where the voting

³² Some letters asked the Commission to clarify the various types of voting arrangements that might be adopted. *See, e.g.*, Letter dated Dec. 21, 2018 from Benjamin Zycher, PhD, American Enterprise Institute at p. 5 (seeking clarification about when it is appropriate to vote proxies).

³³ As we stated in the Fiduciary Interpretation, “[w]hether the disclosure is full and fair will depend upon, among other things, the nature of the client, the scope of the services, and the material fact or conflict. Full and fair disclosure for an institutional client (including the specificity, level of detail, and explanation of terminology) can differ, in some cases significantly, from full and fair disclosure for a retail client because institutional clients generally have a greater capacity and more resources than retail clients to analyze and understand complex conflicts and their ramifications.” (internal citations omitted). *See* Fiduciary Interpretation, 84 FR 33669, at 33677.

recommendation concerns a matter that may present heightened management conflicts of interest or involve a type of matter of particular interest to the investment adviser's client; or

- The investment adviser will vote in favor of all proposals made by particular shareholder proponents. Such an arrangement could be subject to conditions, for example requiring that the shareholder proponent has particular expertise or an investment strategy that will further the interests of the investment adviser's client.
- A client and its investment adviser may agree that the investment adviser would not exercise voting authority in circumstances under which voting would impose costs on the client, such as opportunity costs for the client resulting from restricting the use of securities for lending in order to preserve the right to vote.³⁴
- A client and its investment adviser may agree that the investment adviser will focus voting resources only on particular types of proposals based on the client's preferences, such as proposals relating to corporate events (mergers and acquisition transactions, dissolutions, conversions, or consolidations) or contested elections for directors.
- A client and its investment adviser may agree that the investment adviser would not exercise voting authority on certain types of matters where the cost of voting would be high, or the benefit to the client would be low.³⁵ This could include, for example:

³⁴ We note, however, that the investment adviser would still have to fulfill its duty of loyalty while exercising its voting authority on behalf of its client. For example, an investment adviser must make any determination regarding whether to retain a security and vote the accompanying proxy or lend out the security in the client's best interest.

³⁵ See Proxy Voting Release, 68 FR 6585 at n. 18 and accompanying text.

- Circumstances where the cost of voting the proxy exceeds the expected benefit to the client, including, for example, casting a vote on a foreign security that could involve the additional costs of hiring a translator or traveling to a foreign country to vote the security in person; or
- Circumstances under which casting a vote would not reasonably be expected to have a material effect on the value of the client's investment.

While, as noted above, an investment adviser and its client may shape the voting authority through full and fair disclosure and informed consent, we reiterate that an investment adviser that assumes proxy voting authority must make voting determinations consistent with its fiduciary duty and in compliance with Rule 206(4)-6.³⁶

Question 2: What steps could an investment adviser that has assumed the authority to vote proxies on behalf of a client take to demonstrate that it is making voting determinations in a client's best interest and in accordance with the investment adviser's proxy voting policies and procedures?

Response: As we discuss in Section I above, an investment adviser is a fiduciary and owes each of its clients a fiduciary duty with respect to services undertaken on the client's behalf, including voting. In that discussion, we explain some of the requirements that follow from an investment adviser's fiduciary duty in the context of voting on behalf of clients, including the need for an

³⁶ Rule 206(4)-6 under the Advisers Act requires an investment adviser that assumes proxy voting authority to adopt and implement policies and procedures that are reasonably designed to ensure it votes client securities in the best interest of clients.

investment adviser to conduct a reasonable investigation into matters on which the adviser votes and to vote in the best interest of the client.³⁷

An investment adviser should consider how its fiduciary duty and its obligations under Rule 206(4)-6 apply when it has multiple clients. Many investment advisers have multiple clients, including funds, other pooled investment vehicles, and individual investors, with differing investment objectives and strategies.³⁸ In considering whether an investment adviser's proxy voting policies and procedures are reasonably designed to ensure compliance with Rule 206(4)-6 and to fulfill its fiduciary duty to its clients, an investment adviser should consider whether voting all of its clients' shares in accordance with a uniform voting policy would be in the best interest of each of its clients.³⁹ In particular, where an investment adviser undertakes proxy voting responsibilities on behalf of multiple funds, pooled investment vehicles, or other clients, it should consider whether it should have different voting policies for some or all of these different funds, vehicles, or other clients, depending on the investment strategy and objectives of each.⁴⁰ For example, a growth fund that targets companies with high growth prospects may have

³⁷ The Commission has noted that an investment adviser uses various means of ensuring that proxy votes are voted in its client's best interest and not affected by the adviser's conflicts of interest, in addition to looking to the voting recommendations of a proxy advisory firm. For example, the Commission has stated that "[c]learly, an adviser's policy of disclosing the conflict to clients and obtaining their consents before voting satisfies the requirements of the rule and, when implemented, fulfills the adviser's fiduciary obligations under the Advisers Act.... Other policies and procedures are also available; their effectiveness (and the effectiveness of any policies and procedures) will turn on how well they insulate the decision on how to vote client proxies from the conflict." See Proxy Voting Release, 68 FR 6585, at 6587-88.

³⁸ Such other pooled investment vehicles may include, for example, private funds that are excluded from the definition of investment company by either Section 3(c)(1) or Section 3(c)(7) of the Investment Company Act.

³⁹ Some letters have noted that proxy voting guidelines allow funds to handle efficiently the large majority of votes that are recurring and non-controversial. See, e.g., ICI Letter I at pp. 9-10; ICI Letter II at p. 4.

⁴⁰ As we have noted in the Proxy Voting Release, nothing in Rule 206(4)-6 under the Advisers Act prevents an investment adviser from having different policies and procedures for different clients or different categories of clients. Thus, the board of directors of a fund could adopt and require an investment adviser to use policies and procedures that differ from those the adviser uses with respect to its other clients. Proxy Voting Release, FR 6587 at n. 13.

a different perspective on certain matters submitted to shareholders than an income or dividend fund that seeks to generate an income stream for shareholders in the form of dividends or interest payments.

Funds that invest in voting securities are also required to disclose in their statements of additional information (“SAI”)⁴¹ or on Form N-CSR,⁴² as applicable, the policies and procedures that they use to determine how to vote proxies relating to securities held in their portfolios.⁴³ As discussed above, if the funds have different voting policies and procedures, these should be reflected in the SAI or on Form N-CSR, as applicable.

An investment adviser should also consider whether certain types of matters may necessitate that the adviser conduct a more detailed analysis than what may be entailed by application of its general voting guidelines, to consider factors particular to the issuer or the voting matter under consideration. Such matters might include, but are not limited to, corporate events (mergers and acquisition transactions, dissolutions, conversions, or consolidations) or contested elections for directors. When determining whether to conduct such an issuer-specific analysis, or an analysis specific to the matter to be voted on, an investment adviser should consider the potential effect of the vote on the value of a client’s investments. An investment adviser should consider identifying in its voting policy or policies the factors that it will consider

⁴¹ The SAI is part of a fund’s registration statement and contains information about a fund in addition to that contained in the prospectus. The SAI is required to be delivered to investors upon request and is available on the Commission’s Electronic Data Gathering, Analysis, and Retrieval System (“EDGAR”).

⁴² Form N-CSR is used by open-end funds and closed-end funds to file certified shareholder reports with the Commission on EDGAR.

⁴³ Open-end funds must disclose their proxy voting policies and procedures in their SAIs. Because closed-end funds do not offer their shares continuously, and are therefore generally not required to maintain an updated SAI to meet their obligations under the Securities Act of 1933, they are required to disclose their proxy voting policies and procedures in their annual reports on Form N-CSR. *See* Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, Release No. IC-25922 (Jan. 31, 2003), 68 FR 6564 (Feb. 7, 2003), Form N-1A, Form N-2, Form N-3, and Form N-CSR.

in determining which matters require company-specific evaluation, and how it will evaluate voting decisions on such matters.

In addition, an investment adviser should consider reasonable measures to determine that it is casting votes on behalf of its clients consistently with its voting policies and procedures. For example, one way in which an investment adviser could evaluate its compliance with Rule 206(4)-6 would be to sample the proxy votes it casts on behalf of its clients as part of its annual review of its compliance policies and procedures.⁴⁴ Such a review could specifically include sampling of proxy votes that relate to proposals that may require more issuer-specific analysis (*e.g.*, mergers and acquisition transactions, dissolutions, conversions, or consolidations), to assist in evaluating whether the investment adviser's voting determinations are consistent with its voting policies and procedures and in its client's best interest.⁴⁵

An investment adviser that retains a proxy advisory firm to provide voting recommendations or voting execution services also should consider additional steps to evaluate whether the investment adviser's voting determinations are consistent with its voting policies and procedures and in the client's best interest before the votes are cast. For example, some steps that an investment adviser could use to evaluate its compliance are:

- Sampling pre-populated votes: Where the investment adviser utilizes the proxy advisory firm for either voting recommendations or voting execution (or both), it could assess "pre-populated" votes shown on the proxy advisory firm's electronic voting platform before such votes are cast, such as through periodic sampling of the proxy advisory firm's pre-populated votes.

⁴⁴ See 17 CFR 275.206(4)-7(b) [Rule 206(4)-7(b) under the Advisers Act].

⁴⁵ *Id.*

- Consideration of additional information: Where the investment adviser utilizes the proxy advisory firm for voting recommendations, it could consider policies and procedures that provide for consideration of additional information that may become available regarding a particular proposal. This additional information may include an issuer's or a shareholder proponent's subsequently filed additional definitive proxy materials or other information conveyed by an issuer or shareholder proponent to the investment adviser that would reasonably be expected to affect the investment adviser's voting determination.
- Higher degree of analysis: Where the investment adviser utilizes the proxy advisory firm for either voting recommendations or voting execution (or both), with respect to matters where the investment adviser's voting policies and procedures do not address how it should vote on a particular matter, or where the matter is highly contested or controversial,⁴⁶ it could consider whether a higher degree of analysis may be necessary or appropriate to assess whether any votes it casts on behalf of its client are cast in the client's best interest.

Finally, as part of an investment adviser's ongoing compliance program, the adviser must review and document, no less frequently than annually, the adequacy of its voting policies and procedures to ensure that they have been formulated reasonably and implemented effectively, including whether the applicable policies and procedures continue to be reasonably designed to ensure that the adviser casts votes on behalf of its clients in the best interest of such clients.⁴⁷

⁴⁶ This may include, for example, major acquisitions involving takeovers or contested director elections where a shareholder has proposed its own slate of directors.

⁴⁷ See Proxy Voting Release; *see also* 17 CFR 204-2(a)(17)(ii) [Rule 204-2(a)(17)(ii) under the Advisers Act] (requiring an investment adviser to maintain copies of its records documenting the investment adviser's

Question 3: What are some of the considerations that an investment adviser should take into account if it retains a proxy advisory firm to assist it in discharging its proxy voting duties?

Response: When an investment adviser is considering whether to retain or continue retaining a proxy advisory firm to provide research or voting recommendations as an input to the adviser's voting decisions, we believe that an investment adviser should consider, among other things, whether the proxy advisory firm has the capacity and competency to adequately analyze the matters for which the investment adviser is responsible for voting.⁴⁸ In this regard, investment advisers could consider, among other things, the adequacy and quality of the proxy advisory firm's staffing, personnel, and/or technology.

Such an investment adviser should also consider whether the proxy advisory firm has an effective process for seeking timely input from issuers and proxy advisory firm clients with respect to, for example, its proxy voting policies, methodologies, and peer group constructions, including for "say-on-pay" votes.⁴⁹ For example, if peer group comparisons are a component of

annual review of policies and procedures conducted pursuant to Rule 206(4)-7(b)); Rule 206(4)-7 under the Advisers Act (*e.g.*, requiring investment advisers to adopt and implement written policies and procedures reasonably designed to prevent violation, by the adviser and its supervised person, of the Advisers Act. The rule also requires, among other things, that investment advisers review, no less frequently than annually, the adequacy of their policies and procedures and the effectiveness of their implementation). *See also* Rule 38a-1 under the Investment Company Act (*e.g.*, requiring each fund to adopt and implement written policies and procedures reasonably designed to prevent violation of the federal securities laws by the fund, including policies and procedures that provide for the oversight of compliance by the fund's investment adviser, among others. The rule also requires, among other things, that the fund review, no less frequently than annually, the adequacy of the policies and procedures of the fund and of each investment adviser, principal underwriter, administrator, and transfer agent, and the effectiveness of their implementation).

⁴⁸ In Question No. 4, we provide guidance regarding an investment adviser's duties with respect to evaluating the care and competency of the proxy advisory firm with respect to potential factual errors, potential incompleteness, or potential methodological weaknesses that may materially affect the proxy advisory firm's voting recommendations.

⁴⁹ 17 CFR 240.14a-21 [Rule 14a-21 under the Securities Exchange Act of 1934] requires, among other things, companies soliciting proxies for an annual or other meeting of shareholders at which directors will be

the substantive evaluation, the investment adviser should consider how the proxy advisory firm incorporates appropriate input in formulating its methodologies and construction of issuer peer groups. Where relevant, an investment adviser should also consider how the proxy advisory firm, in constructing peer groups, takes into account the unique characteristics regarding the issuer, to the extent available, such as the issuer's size; its governance structure; its industry and any particular practices unique to that industry; its history; and its financial performance.

Such an investment adviser should also consider whether a proxy advisory firm has adequately disclosed to the investment adviser its methodologies in formulating voting recommendations, such that the investment adviser can understand the factors underlying the proxy advisory firm's voting recommendations.⁵⁰ In addition, the investment adviser should consider the nature of any third-party information sources that the proxy advisory firm uses as a basis for its voting recommendations. The investment adviser also should consider what steps it should take to develop a reasonable understanding of when and how the proxy advisory firm would expect to engage with issuers and third parties.

More generally, an investment adviser's decision regarding whether to retain a proxy advisory firm should also include a reasonable review of the proxy advisory firm's policies and

elected to include a separate resolution subject to a shareholder advisory vote to approve the compensation of named executive officers.

⁵⁰ If an investment adviser utilizes the proxy advisory firm for research and not voting recommendations, it could still evaluate to what extent, if any, the proxy advisory firm's peer group construction methodology may influence how the firm would determine "say-on-pay" votes.

Some letters have called for greater transparency to issuers and clients about the formulation of proxy advisory recommendations and guidelines. *See, e.g.*, Letter dated Oct. 10, 2018 from Timothy M. Doyle, Vice President of Policy and General Counsel, American Council for Capital Formation at p. 2; Letter dated July 26, 2019 from Neil A. Hansen, Vice President, Investor Relations and Corporate Secretary, ExxonMobil at 2 (stating that proxy advisory firms' methodology in evaluating executive compensation can undermine the company's ability to offer incentives for management to pursue long-term shareholder value creation).

procedures regarding how it identifies and addresses conflicts of interest.⁵¹ Some ways in which an investment adviser could conduct this review include, for example, assessing:

- Whether the proxy advisory firm has adequate policies and procedures to identify, disclose, and address actual and potential conflicts of interest, including (1) conflicts relating to the provision of proxy voting recommendations and proxy voting services generally, (2) conflicts relating to activities other than providing proxy voting recommendations and proxy voting services, and (3) conflicts presented by certain affiliations. In the first instance, actual or potential conflicts may include conflicts arising from the provision of recommendations and services to issuers as well as proponents of shareholder proposals regarding matters that may be the subject of a vote. In the third instance, actual or potential conflicts presented by certain affiliations may include whether a third party with significant influence over the proxy advisory firm (*e.g.*, as a shareholder, lender, or significant source of business) has taken a position on a particular voting issue or voting issues more generally;⁵²
- Whether the proxy advisory firm's policies and procedures provide for adequate disclosure (*i.e.*, context-specific, non-boilerplate disclosure) of the proxy advisory firm's actual and potential conflicts with respect to the services the proxy advisory firm provides to the investment adviser. This disclosure could include details on, for example, whether the issuer has received consulting services from the proxy advisory firm, and if

⁵¹ Some letters have noted concerns about proxy advisory firm conflicts of interest. *See, e.g.*, Letter dated Nov. 9, 2018, Business Roundtable; Letter dated Nov. 29, 2018 from Suanne Estatico; Letter dated Jan. 11, 2019 from Darryl M. Burman, Office of the General Counsel, Group 1 Automotive, Inc.

⁵² *See, e.g.*, U.S. Government Accountability Office, Report to Congressional Requesters, Corporate Shareholder Meetings – Issues Relating to Firms That Advise Institutional Investors on Proxy Voting (June 2007).

so, the amount of compensation paid to the firm, if any; whether a proponent of a shareholder proposal or an affiliate of the proponent is or has been a client of the proxy advisory firm; and

- Whether the proxy advisory firm's policies and procedures utilize technology in delivering conflicts disclosures that are readily accessible (for example, usage of online portals or other tools to make conflicts disclosure transparent and accessible).

The steps an investment adviser should take when considering whether to retain or continue retaining a proxy advisory firm could depend on, among other things (1) the scope of the investment adviser's voting authority, and (2) the type of functions and services that the investment adviser has retained the proxy advisory firm to perform. Accordingly, the extent to which an investment adviser takes some or all of the steps described above could vary based on these factors. For example, some of these considerations may be less relevant for an investment adviser that engages a proxy advisory firm solely to execute votes according to detailed voting instructions from the investment adviser, which leaves minimal discretion to the proxy advisory firm. Nevertheless, an investment adviser that retains a proxy advisory firm for this limited purpose should consider what steps to take to understand the proxy advisory firm's own policies and procedures, including its methodologies if applicable, with respect to implementing the investment adviser's voting instructions.

Question 4: When retaining a proxy advisory firm for research or voting recommendations as an input to its voting determinations, what steps should an investment adviser consider taking when it becomes aware of potential factual errors, potential incompleteness, or potential methodological weaknesses in the proxy advisory firm's analysis that may materially affect one

or more of the investment adviser's voting determinations?

Response: As discussed in Section I above, for an investment adviser to form a reasonable belief that its voting determinations are in the best interest of the client, it should conduct a reasonable investigation into the matter. In the case of potential factual errors, potential incompleteness, or potential methodological weaknesses in the proxy advisory firm's analysis, the investment adviser's policies and procedures should be reasonably designed to ensure that its voting determinations are not based on materially inaccurate or incomplete information. For example, an investment adviser that has retained a proxy advisory firm for research or voting recommendations as an input to its voting determinations should consider including in its policies and procedures a periodic review of the investment adviser's ongoing use of the proxy advisory firm's research or voting recommendations. Such a review could include an assessment of the extent to which potential factual errors, potential incompleteness, or potential methodological weaknesses in the proxy advisory firm's analysis (that the investment adviser becomes aware of and deems credible and relevant to its voting determinations) materially affected the proxy advisory firm's research or recommendations that the investment adviser utilized.

In reviewing its use of a proxy advisory firm, an investment adviser should also consider the effectiveness of the proxy advisory firm's policies and procedures for obtaining current and accurate information relevant to matters included in its research and on which it makes voting recommendations. As part of this assessment, investment advisers should consider, and in certain cases may wish to communicate with proxy advisory firms, regarding the following:

- The proxy advisory firm's engagement with issuers, including the firm's process for ensuring that it has complete and accurate information about the issuer and each

particular matter, and the firm's process, if any, for investment advisers to access the issuer's views about the firm's voting recommendations in a timely and efficient manner;

- The proxy advisory firm's efforts to correct any identified material deficiencies in the proxy advisory firm's analysis;
- The proxy advisory firm's disclosure to the investment adviser regarding the sources of information and methodologies used in formulating voting recommendations or executing voting instructions;⁵³ and
- The proxy advisory firm's consideration of factors unique to a specific issuer or proposal when evaluating a matter subject to a shareholder vote.

Question 5: How can an investment adviser evaluate the services of a proxy advisory firm that it retains, including evaluating any material changes in services or operations by the proxy advisory firm?

Response: In order to act consistently with Rule 206(4)-6, an investment adviser that has retained a third party (such as a proxy advisory firm) to assist substantively with its proxy voting responsibilities and carrying out its fiduciary duty should adopt and implement policies and procedures that are reasonably designed to sufficiently evaluate the third party in order to ensure that the investment adviser casts votes in the best interest of its clients.⁵⁴

For example, a proxy advisory firm's business and/or its policies and procedures regarding conflicts of interest could change after an investment adviser's initial assessment of the

⁵³ See Question No. 3 above.

⁵⁴ See *supra* at n. 47.

proxy advisory firm, and these changes could, for example, materially alter the effectiveness of the proxy advisory firm's policies and procedures and may require the investment adviser to make a subsequent assessment. In this regard, we believe that investment advisers that retain a proxy advisory firm to provide research or voting recommendations (or both) should consider policies and procedures to identify and evaluate a proxy advisory firm's conflicts of interest that can arise on an ongoing basis, in addition to updates regarding the proxy advisory firm's capacity and competency to provide voting recommendations or to execute votes in accordance with an investment adviser's voting instructions.⁵⁵ Accordingly, the investment adviser should consider requiring the proxy advisory firm to update the investment adviser regarding business changes the investment adviser considers relevant (*i.e.*, with respect to the proxy advisory firm's capacity and competency to provide independent proxy voting advice or carry out voting instructions). An investment adviser should also consider whether the proxy advisory firm appropriately updates its methodologies, guidelines, and voting recommendations on an ongoing basis, including in response to feedback from issuers and their shareholders.

Question 6: If an investment adviser has assumed voting authority on behalf of a client, is it required to exercise every opportunity to vote a proxy for that client?

Response: No, if either of two situations applies. First, if an investment adviser and its client have agreed in advance to limit the conditions under which the investment adviser would exercise voting authority, as discussed above, the investment adviser need not cast a vote on behalf of the client where contemplated by their agreement.

⁵⁵

Id.

Second, as the Commission has stated previously, there may be times when an investment adviser that has voting authority may refrain from voting a proxy on behalf of a client if it has determined that refraining is in the best interest of that client.⁵⁶ This may be the case where the adviser determines that the cost to the client of voting the proxy exceeds the expected benefit to the client.⁵⁷ In making such a determination, the investment adviser may not ignore or be negligent in fulfilling the obligation it has assumed to vote client proxies and cannot fulfill its fiduciary responsibilities to its clients by merely refraining from voting the proxies.⁵⁸ Accordingly, before refraining from voting under the circumstances described in this second situation, an investment adviser should consider whether it is fulfilling its duty of care to its client in light of the scope of services to which it and the client have agreed.

III. OTHER MATTERS

Pursuant to the Congressional Review Act,⁵⁹ the Office of Information and Regulatory Affairs has designated this guidance as not a “major rule,” as defined by 5 U.S.C. 804(2).

List of Subjects in 17 CFR Parts 271 and 276

Securities.

⁵⁶ See Proxy Voting Release, 68 FR 6585, at 6587. We also have stated that “[w]hether the advice is in a client’s best interest must be evaluated in the context of the portfolio that the adviser manages for the client and the client’s objectives.” See Fiduciary Interpretation, 84 FR 33669, at 33673.

⁵⁷ See Proxy Voting Release, 68 FR 6585, at 6587. The Commission stated in that release that “we do not suggest that an adviser that fails to vote every proxy would necessarily violate its fiduciary obligations. There may even be times when refraining from voting a proxy is in the client’s best interest, such as when the adviser determines that the cost of voting the proxy exceeds the expected benefit to the client.” *Id.* In this second situation, the costs to be considered would necessarily have to be additional costs to the client.

⁵⁸ See 68 FR 6585, at 6587-88.

⁵⁹ 5 U.S.C. 801 *et seq.*

Amendments to the Code of Federal Regulations

For the reasons set out above, the Commission is amending title 17, chapter II of the Code of Federal Regulations as set forth below:

PART 271 – INTERPRETATIVE RELEASES RELATING TO THE INVESTMENT COMPANY ACT OF 1940 AND GENERAL RULES AND REGULATIONS THEREUNDER

1. An authority citation is added for part 271 to read as follows:

Authority: 15 U.S.C. 80a *et seq.*

2. The table is amended by adding an entry for Release No. IC-33605 at the end to read as follows:

Subject	Release No.	Date	Fed. Reg. Vol. and Page
** Commission Guidance Regarding the Proxy Voting Responsibilities of Investment Advisers	* IC-33605	** August 21, 2019	** [Insert FR Volume Number] FR [Insert FR Page Number]

**PART 276 – INTERPRETATIVE RELEASES RELATING TO THE INVESTMENT
ADVISERS ACT OF 1940 AND GENERAL RULES AND REGULATIONS
THEREUNDER**

3. An authority citation is added for part 276 to read as follows:

Authority: 15 U.S.C. 80b *et seq.*

4. The table is amended by adding an entry for Release No. IA-5325 at the end to read as follows:

Subject	Release No.	Date	Fed. Reg. Vol. and Page
** Commission Guidance Regarding the Proxy Voting Responsibilities of Investment Advisers	* IA-5325	** August 21, 2019	** [Insert FR Volume Number] FR [Insert FR Page Number]

By the Commission.

Dated: August 21, 2019.

Vanessa A. Countryman,
Secretary.

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