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Submitted to the U.S. House of Representatives Committee on Financial Services
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Markup of H.R. 5983, the "Financial CHOICE Act of 2016"

GLASS LEWIS

To Chairman Hensarling, Ranking Member Waters and members of the Committee on Financial Services:

Glass, Lewis & Co. ("Glass Lewis"), a leading independent provider of governance services and a founding signatory to the Best Practice Principles for Shareholder Voting Research, appreciates the opportunity to submit this statement for the record in today's markup of H.R. 5983, the "Financial CHOICE Act of 2016." The following statement relates to Title X-Subtitle Q, "Corporate Governance Reform and Transparency," of the proposed legislation.

H.R. 5983 Title X-Subtitle Q, if enacted, would significantly hinder the ability of proxy advisory firms to deliver independent research and analysis in a cost-effective and timely manner to institutional investor clients, thereby compromising the ability of institutional investors to fulfill their fiduciary duties.

Statement Summary

Institutional investors have a fiduciary responsibility to vote the proxies of their public company holdings in the best interests of beneficiaries. As such, it is prudent and within their rights for investors to avail themselves of the resources they deem appropriate to fulfill that fiduciary obligation.

Glass Lewis is dedicated to helping institutional investors better understand and connect directly with the companies in which they invest. Our duty, as a proxy advisory firm, is to support – not usurp – the role of our clients as investors/owners, a distinction we take very seriously. It is reflected in how we develop and update our policies, create our research, and engage with companies, shareholders and other stakeholders.

Glass Lewis' core business is providing independent research and recommendations – derived exclusively from publicly-available information; developed in accordance with the policy or policies selected by the client; and delivered in a timely fashion – so investors can effectively fulfill their fiduciary responsibilities. (Glass Lewis does not offer consulting services to corporate issuers, directors, dissident shareholders or shareholder proposal proponents.)

As participants in the securities industry, all proxy advisory firms are subject to the antifraud provisions of the federal securities laws, including laws and regulations prohibiting trading on the basis of material non-public information (insider trading) and market manipulation. Proxy advisory firms also are subject to the Securities and Exchange Commission's proxy solicitation rules under the Securities Exchange Act of 1934 ("Exchange Act"). Rule 14a-2 under the Exchange Act provides certain exemptions on which a proxy voting advisor may rely, provided it meets the conditions set forth in the rule. Commercial proxy voting advisors operating today, including Glass Lewis, are generally deemed by the SEC as qualifying for the exemptions based on rules 14a-2(b)(1) and 14a-2(b)(3).[1]

Proxy advisory firms perform a necessary and valuable function, supporting clients' vote management processes across potentially thousands of holdings – collecting, translating and distilling public disclosure; developing recommendations based on clients' specified policy or policies; and transmitting votes based on how each client directs. However, investor clients at all times retain control of and responsibility for their voting decisions.

In Staff Legal Bulletin No. 20 IM/CF ("SLB 20"), the SEC clearly states investment advisers that retain the services of a proxy advisory firm are responsible for overseeing their service providers to ensure proxies are being voted in the best interests of the investment advisers' clients. Further, SLB 20 specifies that investment advisers are responsible for ascertaining whether their proxy advisory firm(s) has the capacity and competency to adequately analyze proxy issues. In particular, investment advisers are expected to assess "the adequacy and quality

[1] See 14a-2(b)(1) and 14a-2(b)(3) under the Securities Exchange Act of 1934 ("Exchange Act"), https://www.sec.gov/about/laws/sea34.pdf.

of the proxy advisory firm's staffing and personnel; the robustness of its policies and procedures regarding its ability to (i) ensure that its proxy voting recommendations are based on current and accurate information and (ii) identify and address any conflicts of interest and any other considerations that the investment adviser believes would be appropriate in considering the nature and quality of the services provided by the proxy advisory firm."[2]

In 2015, the Investment Company Institute (ICI), the leading industry association for the mutual fund industry, published the "Report on Funds' Use of Proxy Advisory Firms," which clearly defines the obligations and responsibilities of investment companies ("funds"), fund boards of directors and fund advisers with respect to the selection and oversight of proxy advisory firms:

> *"A fund's board of directors, acting on behalf of the fund, is responsible for the voting of proxies relating to the fund's portfolio securities. A fund's board typically delegates proxy voting responsibilities to the fund's investment adviser in recognition that proxy voting is part of the investment management process. While the nature and extent of this delegation may vary, it remains subject to the board's continuing oversight. When a fund adviser votes proxies, it must do so in a manner consistent with its own fiduciary duties to the fund. … In addition, a fund adviser must adopt and implement policies and procedures reasonably designed to ensure that it votes proxies in the best interest of the fund."*[3]

As the ICI noted in its letter regarding the Corporate Governance Reform and Transparency Act of 2016 (now Title X-Subtitle Q of H.R. 5983), assessing the adequacy of proxy advisory firms' financial and managerial resources is a task better undertaken by mutual funds themselves: "Fund advisers have long understood the importance of conducting due diligence and ongoing oversight of all key service providers, including proxy advisory firms. … Funds and fund advisers

[2] See Securities and Exchange Commission Staff Legal Bulletin No. 20 (IM/CF), June 30, 2014, https://www.sec.gov/interps/legal/cfslb20.htm.
[3] "Report on Funds' Use of Proxy Advisory Firms," Independent Directors Council and the Investment Company Institute, January 2015.

have legal and economic incentives – and the expertise – to evaluate proxy advisory firms' capacity and competency in providing proxy voting services."[4]

Glass Lewis has always provided clients with the necessary information about the firm's resources, personnel, service levels, research policies and procedures, business continuity and viability, error management, and conflict management policies and procedures, etc. Following the publication of SLB 20, Glass Lewis has been subject to even more frequent client-led due diligence exams regarding those matters, including queries about our independence and the support we receive from our owners.

The concerns surrounding the influence of proxy advisory firms on voting behavior, as reflected in the "Corporate Governance Reform and Transparency" section of H.R. 5983, are based on false and outdated information regarding the influence of proxy advisory firms and a mischaracterization of how investors use proxy advisory firms. The push for more regulation reflects a lack of understanding of how proxy advisory firms develop their research and recommendations, communicate with subject companies and other stakeholders, and manage and disclose conflicts of interests – despite the fact that proxy advisory firms are clearly, comprehensively and consistently disclosing information regarding all these subjects on their public websites and in their Statements of Compliance to the Best Practice Principles for Shareholder Voting Research[5].

1. <u>Proposed Legislation Rests on False Premise About Proxy Advisor Influence</u>

Claims about the influence on voting outcomes of proxy advisory firm advice are not supported by consistent, reliable evidence and are belied by actual vote results: While Glass

[4] ICI letter to Chairman Carney and Representative Duffy, Corporate Governance Reform and Transparency Act of 2016, June 13, 2016.
[5] See "Best Practice Principles for Shareholder Voting Research" (March 2014) and Statements of Compliance of signatories to the Principles; https://bppgrp.info/; https://bppgrp.info/signatory-statements/.

Lewis recommended against between 13%-17% of advisory compensation votes since the adoption of the rule in 2010, only about 2% of such proposals are defeated each year. According to the 2012 study by Tapestry Networks and the IRRC Institute, proxy advisory firm guidelines and recommendations are used by investors in different ways. Most respondents to the study said they employ custom policies and may use proxy advisory firm recommendations as "a point of reference."[6] Further, while some investors may have been more inclined to be guided or follow a proxy advisory firm's recommendations in the past, there has been a clear trend toward more customization of voting decisions. The policies of proxy advisory firms, for the most part, reflect the approaches of their clients.

Proxy advisory firms cannot control whether a client is following its recommendation, votes the same way for different reasons or is voting differently than the recommendation. Indeed, the SEC made it very clear in SLB 20 that the fiduciary duty of care and loyalty with respect to proxy voting responsibilities rests with the investors.[7]

The majority of Glass Lewis' clients, like the vast majority of the world's largest pension funds and asset managers, vote according to their own custom voting policies. Even the minority of clients who generally tend to follow the Glass Lewis policy often override the Glass Lewis recommendation in favor of their own voting decision, including nearly 10% of the time for proposals on political contribution disclosure and for almost 15% of proposals to separate the roles of chairman and CEO (May 1, 2015-April 30, 2016).

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[6] Voting Decisions at US Mutual Funds: How Investors Really Use Proxy Advisers, Tapestry Networks and IRRC Institute, Robyn Bew and Richard Fields (June 2012).

[7] Division of Investment Management, Division of Corporation Finance, Securities and Exchange Commission; Proxy Voting: Proxy Voting Responsibilities of Investment Advisers and Availability of Exemptions from the Proxy Rules for Proxy Advisory Firms; Staff Legal Bulletin No. 20 (IM/CF); Publication of IM/CF Staff Legal Bulletin; June 30, 2014.

2. Proposed Legislation Favors Corporate Interests Over Investor Interests

H.R. 5983 Title X-Subtitle Q will require proxy advisory firms to give away research to companies (which investors have to pay for) and to meet with companies prior to issuing reports – potentially subjecting the proxy advisory firms to corporate lobbying on issues like executive compensation ("say on pay") and board entrenchment. These provisions would make it impossible for investors to rely on the independence and timeliness of proxy advisory firm research.

3. Existing Regulation Already Addresses Concerns Regarding Proxy Advisors

a) Regulation and Self-Regulation Frameworks Already Exist

In the past several years, a number of regulatory bodies in the United States and elsewhere, including the SEC, Canadian Securities Administrators (CSA) and European Securities and Markets Authority (ESMA), have examined the role of proxy advisory firms and whether they should be subject to various forms of regulation.

In every single case, these regulators have chosen not to impose new regulations on proxy advisory firms. Instead, they have emphasized the role of existing regulations that are already on the books in ensuring that investors and the capital markets are adequately protected, and the role of the private sector in establishing and enforcing appropriate standards of conduct for proxy advisory firms. In the United States, while proxy advisory firms are not required by the SEC to register under the Investment Advisers Act, they are subject to various provisions of the federal securities laws and regulations, depending on the nature of their activities. In particular, in SLB 20, the SEC reaffirmed the staff's view that proxy advisory firms are able to operate under an exemption to Exchange Act Rule 14a-2(b)(3). The exemption requires disclosure of "any significant relationship" the proxy firm has with the issuer, its affiliates, or a shareholder proponent of a matter on which it provides voting advice.

Both ESMA and the CSA, in publishing the findings of their respective industry reviews, stated that binding or quasi-binding regulation of proxy advisory firms was not warranted and recommended the creation of an industry code of conduct. According to ESMA: "In its efforts to intensify its work on corporate governance issues, ESMA has undertaken an extensive analysis of the proxy advisory industry in the EU, with input from users, providers and issuers, and has found no evidence of a market failure requiring regulatory intervention."

In response to global regulatory reviews and in accordance with ESMA's stated recommendations, a number of the world's largest providers of proxy advisory services, including Glass Lewis and ISS, formed an industry group (the Best Practice Principles for Shareholder Voting Research Group, or "BPPG"). The BPPG, under the oversight of an independent chair funded by ESMA, developed and instituted a code of conduct for firms that offer proxy advisory services, comprising a set of best practice principles and related guidance.

The code of conduct, known as the "Best Practice Principles for Shareholder Voting Research," focuses on two key areas: 1) identifying, disclosing and managing conflicts of interest; and 2) fostering transparency to ensure the accuracy and reliability of the advice offered by proxy advisory firms through disclosure of general voting policies and methodologies and information on engagement with issuers, other stakeholders and the media.

As signatories to the Best Practice Principles for Shareholder Voting Research, Glass Lewis and other proxy advisory firms are required to disclose publicly how they comply, in relation to their business activities globally, with the Principles and associated guidance. In the event that a signatory does not comply with one or more elements of the industry code, the signatory must provide a detailed explanation. Signatory statements of compliance to the industry code of conduct are publicly available at the BPPG website (www.bppg.info), as well as on the signatories' own websites.

b) Proxy Advisory Firms Already Publicly Disclose Policies and Methodologies

Glass Lewis is fully transparent about its policies and procedures for analyzing companies, publicly disclosing significant information about its research policies and approach, including the unabridged guidelines for the analysis of U.S. companies, as well as the voting guidelines for other major countries. This information can be accessed via Glass Lewis Issuer Engagement Portal at http://www.glasslewis.com/issuer-overview/. In addition, Glass Lewis' public Statement of Compliance with the Best Practice Principles for Shareholder Voting Research contains substantially more information about the Glass Lewis research approach and methods, including statistics on voting recommendations in conflicted situations. The Statement of Compliance also outlines how Glass Lewis develops its proxy voting policies: http://www.glasslewis.com/best-practices-principles/.

c) Proxy Advisory Firms Already Manage and Disclose Potential Conflicts of Interest

The proxy advisory industry, including Glass Lewis, already complies with the provisions proposed in H.R. 5983 regarding conflict management, disclosure and oversight. Glass Lewis eliminates, reduces and discloses – proactively, explicitly and comprehensively – potential conflicts. Glass Lewis does not provide consulting services to public companies or directors, nor do we provide consulting to shareholders regarding how to gain support from other shareholders for their proposals or dissident nominees in a proxy contest. The firm has a robust and publicly-disclosed conflicts policy that governs the disclosure and treatment of the firm's various types of potential conflicts, including those arising from the firm's ownership structure, business partnerships, clients, employees and outside advisor relationships. Glass Lewis has, since its founding, disclosed potential conflicts of all types prominently and specifically in each report.

Further, Glass Lewis maintains a robust code of ethics that addresses personnel conflicts, confidential treatment of client information and insider trading, among many other topics. All Glass Lewis employees and agents, worldwide, must annually review and affirm their commitment to the Glass Lewis Code of Ethics, as well as update Glass Lewis with information on (i) any reportable outside activities (e.g. other employment, involvement in investment clubs, etc.) or any other activities related to the securities industry or the business of Glass Lewis, and (ii) any ownership interest greater than 5% or any position (e.g. director, officer or executive) the employee or agent, or any of his or her relatives, holds in a publicly-traded company. Glass Lewis' Compliance Committee, which meets quarterly, regularly reviews the Code of Ethics and incorporates any revisions required by applicable laws, rules and regulations. In addition, the Vice President and General Counsel, who serves as the firm's Chief Compliance Officer, monitors the disclosure of personal trading accounts, the pre-approval trading process, and all employees' and agents' quarterly personal trading reporting.

Glass Lewis is transparent about ownership and operates as an independent company separate from its owners, the Ontario Teachers' Pension Plan Board ("OTPP") and Alberta Investment Management Corp. ("AIMCo"); neither owner is involved in the day-to-day management of Glass Lewis' business. Moreover, Glass Lewis excludes OTPP and AIMCo from any involvement in the formulation and implementation of its proxy voting policies and guidelines, and in the determination of voting recommendations for specific shareholder meetings.

As detailed on the company website (http://www.glasslewis.com/conflict-of-interest/), Glass Lewis has a formal Conflict of Interest Statement, Conflict Management Procedures, Code of Ethics and several additional safeguards in place to mitigate potential conflicts.

d) Proxy Advisory Firms Already Communicate With Companies & Disclose Communication Policy

Proxy advisory firms allow companies to fact-check reports: In 2015, Glass Lewis launched a program to provide subject companies, at no charge to the companies, the opportunity to review the facts and data used in drafting reports prior to Glass Lewis completing its analysis and publishing reports for investor clients. Issuers can check the accuracy of data, via the Issuer Data Report ("IDR") service, and have the opportunity to notify Glass Lewis of any issues prior to Glass Lewis completing its analysis. In 2016, Glass Lewis provided 500 US companies of varying sizes with their IDR, double the number produced in 2015. Glass Lewis will continue to expand this program in the coming years until it can provide an IDR – for free – to all companies it covers, irrespective of company size.

Proxy advisory firms have robust systems to address purported factual errors or omissions: Issuers can submit queries and notifications of subsequent filings and additional information, as well as what they perceive to be errors, via the public Issuer Engagement Portal. When Glass Lewis is notified of a purported error, we immediately review the report. If there is a reasonable likelihood the report will require revising, the report is removed from its published status so no additional clients can access it. For the 12 months ending April 30, 2016, material errors in Glass Lewis' research (brought to our attention by the company, its advisors or through subsequent disclosure) that resulted in a change to the Glass Lewis recommendation represented one-tenth of 1% of the items up for vote at US companies analyzed by Glass Lewis. (In each of the circumstances where an error resulted in a change to the Glass Lewis recommendation, we were able to publish the change and notify clients with enough time to evaluate the revised report prior to the vote cutoff.)

Proxy advisory firms meet with companies when appropriate: Proxy advisory firms have different policies regarding communication with subject companies. These policies are publicly disclosed on proxy advisory firm websites and in proxy advisory firms' Statements of Compliance to the Best Practice Principles for Shareholder Voting Research. The manner in which a proxy advisory firm communicates with issuers is among the activities that investors consider when selecting a proxy advisor. It's important to remember that proxy advisory firms are not shareholders. Unless the proxy advisory firm provides "engagement" services to investors, they are not empowered by clients to negotiate on their behalf for specific changes to governance practices or structures at investee companies.

Glass Lewis believes that discussions with issuers and their representatives, at the appropriate time, foster mutual understanding and promote better disclosure. As a general policy, we do not discuss our policies or recommendations with issuers during the solicitation period (which begins on the date the notice of meeting is released and ends on the date of the meeting), mitigating the risk of inappropriate influence from companies on recommendations. We sometimes conduct a "Proxy Talk" conference call with companies, which we record for access by our clients. However, we will engage with companies during the solicitation period, if necessary, to discuss purported factual errors or omissions in our reports.

4) The Proposed Legislation Would Hurt Long-Term Savers

Not only is the Corporate Governance and Reform section of H.R. 5983 unnecessary, its passage would have dire consequences for the nation's pension plan participants, mutual fund investors and other long-term savers, as it would: 1) deny investors access to independent research by requiring proxy advisory firms to submit to corporate influence on issues like executive compensation and board elections prior to completing the analysis for their investor clients; 2) severely limit the time investors have to properly consider the analysis in developing informed proxy voting decisions; and 3) result in higher costs for institutional investors and their beneficiaries.

The proposed legislation would infringe upon Glass Lewis' ability to independently analyze the issues requiring a shareholder vote and to make unbiased voting recommendations to its clients by requiring that Glass Lewis provide drafts of its recommendations to issuers before publication, make its employees available to issuers to lobby for changes to its recommendations, and resolve any issuer complaints about its recommendations before the voting deadline. The result would be to increase conflicts of interest in the industry, which is contrary to the intent of the legislation and the expectations of our clients.

This provision also would increase the likelihood that proxy advisory firms would be unable to conduct their analyses and publish their reports to clients in a timely manner, so that clients can consider the research before voting. Most U.S. companies hold their annual meetings between March and May, and file their definitive proxy statement six weeks to eight weeks before the meeting. Furthermore, H.R. 5983 features anti-competitive requirements for proxy advisory firms that would both significantly increase the barriers to entry for new participants in the industry and make it very difficult for existing participants to survive. These provisions include such things as requiring a proxy advisory firm to disclose its financial condition and client list, both highly sensitive pieces of proprietary business information that have no bearing on the investor protection issues that the proposed legislation purports to address.

H.R. 5983 also would force proxy advisory firms to give away for free their reports and models used to analyze issues up for vote – proxy advisory firms' valuable intellectual property – in order to facilitate issuers being able to lobby for changes to recommendations. In no other part of the financial services industry does the law or regulation require a company to give away its valuable intellectual property for free. Forcing proxy advisory firms to facilitate the free distribution of their intellectual property would impact revenues and raise costs – with no concomitant benefits from the perspective of clients – which would require proxy advisory firms to raise prices, adjust operations and/or take other steps that may be detrimental to investors who rely on proxy advisory firms as a source of information to assist them in exercising their rights as shareholders.

Rather than restricting or eliminating competition in this field, Congress should foster an environment where it will be possible for new businesses to enter this field and offer alternative points of view for the benefit of investors. Investor consumers of proxy advisory services hold their advisors accountable and are satisfied with the current system; it is telling that the call for regulating advisors is coming not from investors but from the companies that are the subject of the advisors' reports.

Investors and pension plan beneficiaries, such as teachers, police officers and firefighters, rely on mutual fund and pension fund officers to prudently and cost-effectively manage their investment assets; this includes making informed voting decisions at the shareholder meetings of public companies in their investment portfolios. This onerous regulation would raise the costs for the investment professionals in fulfilling their fiduciary responsibility to make voting decisions, and those higher costs would be passed through to investors and beneficiaries.

5) Investors Oppose the Legislation

Investor organizations and individual institutional investors, including the ICI, the Council of Institutional Investors (CII), the International Corporate Governance Network (ICGN), California State Teachers Retirement System, Ohio Public Employees Retirement System, Florida State Board of Administration, the Washington State Investment Board and the United Nations-supported Principles for Responsible Investment (PRI), among others, have expressed publicly their opposition to the legislation.

The CII, an association mainly of employee benefit plans, warned the proposed legislation "could weaken public company corporate governance in the United States; lessen the fiduciary obligation of proxy advisory firms to investor clients; and reorient any surviving proxy advisory firms to serve companies rather than investors." The ICI in its letter regarding the Corporate Governance Reform and Transparency Act of 2016 said it was "skeptical about the need for a comprehensive, new regulatory regime for proxy advisory firms that would likely result in increased costs for mutual funds and our shareholders with little to no corresponding benefits."[8]

Conclusion

H.R. 5983 Title X-Subtitle Q will compromise the ability of pension funds, mutual funds, asset managers and hedge funds to properly fulfill their fiduciary duties. We believe the existing regulatory framework, oversight by investors and adherence to a global code of best practices has proven to be effective to ensure the quality and research of proxy advisory firms without adding undue costs to investors or inhibiting competition.

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Thank you Mr. Chairman and Ranking Member Waters for considering these views. Glass Lewis appreciates the opportunity to submit this statement.

Sincerely,

Katherine Rabin
Chief Executive Officer

[8] ICI letter to Chairman Carney and Representative Duffy, Corporate Governance Reform and Transparency Act of 2016, June 13, 2016