

# SEC Releases Guidance on Proxy Voting and Use of Proxy Advisory Firms

July 9, 2014

On June 30, 2014, the Securities and Exchange Commission (SEC) issued Staff Legal Bulletin No. 20 (Bulletin), which clarifies the responsibilities of registered investment advisers when voting client proxies and retaining proxy advisory firms.<sup>[1]</sup> Investment advisers should note that while the SEC staff acknowledged that investment advisers may need to implement changes in light of the Bulletin, it also stated that any such changes are expected to be made prior to next year's proxy season.

Rule 206(4)-6 of the Investment Advisers Act of 1940 (Proxy Voting Rule) requires a registered investment adviser, among other things, to adopt and implement written policies and procedures reasonably designed to ensure that the investment adviser votes proxies in the best interest of its clients.<sup>[2]</sup> To ensure compliance with the Proxy Voting Rule, the Bulletin recommended that investment advisers periodically sample proxy votes, including proxy votes relating to proposals that require more analysis, and review whether they comply with the investment advisers' proxy voting policies and procedures. In addition, investment advisers should review, at least annually, the adequacy of their proxy voting policies and procedures to determine if such policies and procedures have been implemented effectively and if proxies have been voted in the best interests of clients.

The Bulletin emphasized that investment advisers are not required to vote every proxy in order to satisfy the Proxy Voting Rule. Instead, investment advisers and their clients have flexibility in determining the scope of the investment advisers' proxy voting responsibilities and any delegation thereof. The Bulletin offered several examples of how an investment adviser and its client may agree to tailor their proxy voting arrangements, including agreements for the investment adviser to:

(i) Abstain from certain types of proposals due to time and costs constraints;

- (ii) Abstain from voting any proxies at all, regardless of whether the client undertakes to vote the proxies itself;
- (iii) Vote proxies as recommended by the issuer's management or a particular shareholder proponent, absent client instructions to the contrary; and
- (iv) Focus resources on only particular types of proposals based on the client's preferences.

Investment advisers may also engage proxy advisory firms to provide recommendations on voting client proxies. However, prior to retaining or continuing to retain a proxy advisory firm, investment advisers should consider whether the proxy advisory firm has the capacity and competency to analyze proxy issues adequately. Relevant factors include the adequacy and quality of the proxy advisory firm's staffing and personnel, as well as the robustness of the proxy advisory firm's policies and procedures regarding its ability to (i) ensure that proxy voting recommendations are based on current and accurate information and (ii) identify and address any conflicts of interest.

The Bulletin also made clear that investment advisers have an ongoing duty to oversee proxy advisory firms they have retained. Investment advisers should implement policies and procedures reasonably designed to ensure sufficient oversight and identify any conflicts of interest of proxy advisory firms that may arise on an ongoing basis. This may include requiring the proxy advisory firm to notify the investment adviser of any business changes and any policies and procedures relating to conflicts of interest. Moreover, if the investment adviser determines that a proxy advisory firm's recommendation is based on a material factual error, the investment adviser should investigate the error and ascertain whether the proxy advisory firm is taking reasonable steps to reduce similar errors in the future.

If you have any questions concerning the Bulletin or the Proxy Voting Rule in general, please contact your regular Proskauer lawyer or any of the Proskauer lawyers listed in this alert. [\[1\]](#) The Bulletin was jointly issued by the Division of Investment Management and the Division of Corporation Finance and consists of thirteen questions and answers. The Bulletin also addressed exemptions from federal proxy rules available to proxy voting firms, a topic which is not covered in this alert. A copy of the Bulletin can be found on the SEC's website [here](#).

[\[2\]](#) Under the Proxy Voting Rule, it is a fraudulent, deceptive, or manipulative act, practice or course of business within the meaning of Section 206(4) of the Advisers Act for a registered investment adviser to exercise voting authority with respect to client securities, unless (i) the adviser has adopted and implemented written policies and procedures that are reasonably designed to ensure that the adviser votes proxies in the best interest of its clients, (ii) the adviser describes its proxy voting procedures to clients and provides copies on request, and (iii) the adviser discloses to clients how they may obtain information on how the adviser voted their proxies.

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