



SEC Guidance on Proxy Voting for Investment Advisers and Proxy Advisory Firms

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Investment Adviser Obligations

The new guidance provides steps that investment advisers can take to demonstrate that proxy votes are cast in accordance with clients' best interests. These steps could include (1) periodically sampling proxy votes to review whether they complied with the adviser's proxy voting policies and procedures and (2) reviewing a sample of proxy votes relating to certain proposals that may require more analysis. In addition, the investment adviser should review its proxy voting policies and procedures no less frequently than annually to ensure adequate implementation and design.

The guidance also clarifies that an investment adviser is not obligated to vote every proxy and that the delegation of client voting authority may include several arrangements, such as:

- an agreement that the time and cost associated with the mechanics of voting proxies of certain types of proposals may not be in the client's best interest
- an agreement that the adviser should vote as recommended by management or a particular shareholder proponent
- an agreement to abstain from voting any proxies
- an agreement to focus only on specific types of proposals.

Finally, the SEC set forth guidance for investment advisers when retaining proxy advisory firms, including that an adviser should ascertain whether the proxy advisory firm has the capacity and competency to adequately analyze proxy issues. This could include, for example, an analysis of the advisory firm's ability to (1) ensure that its recommendations are based on current and accurate information and (2) identify and address any conflicts of

interest. In addition, the guidance requires that an investment adviser adopt policies and procedures for oversight of retained proxy advisory firms. The SEC added that if a proxy advisory firm makes an error, the investment adviser should investigate the error and confirm whether the proxy advisory firm is taking steps to reduce future errors.

Proxy Advisory Firm Obligations

The SEC guidance also addresses situations in which a proxy advisory firm would be subject to the federal proxy rules by engaging in a proxy “solicitation.” The guidance confirms that “providing recommendations that are reasonably calculated to result in the procurement, withholding or revocation of a proxy would subject a proxy advisory firm to the proxy rules.”

In addition, the guidance addresses the availability to proxy advisory firms of certain exemptions from the proxy rules’ information and filing requirements. Rule 14a-2(b)(1) of the Exchange Act provides an exemption from most provisions of the proxy rules for solicitations by a person who does not at the same time seek the power to act as a proxy for a shareholder and does not furnish or request a form of revocation, abstention, consent or authorization. Under the new SEC guidance, a proxy advisory firm would not be able to rely on the exemption provided by Rule 14a-2(b)(1) if it allowed a client to establish, in advance of receiving proxy materials for a particular shareholder meeting, general policies that the proxy advisory firm would apply in its discretion to vote on behalf of the client. On the other hand, a proxy advisory firm could rely on the exemption in Rule 14a-2(b)(1) if it only distributes reports containing recommendations.

The guidance also clarifies that the exemption in Rule 14a-2(b)(3) would be available to a proxy advisory firm in situations in which the firm has an existing business relationship with the recipient of the firm’s advice, subject to certain conditions, including that the firm discloses to the recipient any significant relationship between the proxy advisory firm and the company or a shareholder proponent of a matter upon which advice is being given, as well as any material interest of the firm. The guidance adds that this disclosure is an affirmative duty of the proxy advisory firm that cannot be satisfied by merely stating that the information regarding significant relationships or material interests will be provided upon request.

The SEC expects that any changes to the policies of an investment adviser or proxy advisory firm in reaction to the guidance be implemented promptly, but in any event by next year’s proxy season.

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