Securities and Exchange Commission Investor Advisory Committee
Minutes of the Meeting on Sept. 13, 2018

The Investor Advisory Committee (IAC) met on September 13, 2018, in a public meeting at the Securities and Exchange Commission's headquarters in Washington, D.C. The meeting convened shortly after 9 a.m. and was broadcast live by webcast.

The following persons participated in the meeting:

Commissioners of the Securities and Exchange Commission
Chairman Jay Clayton (morning only)
Commissioner Kara Stein (morning only)
Commissioner Robert Jackson, Jr. (afternoon only)
Commissioner Hester Peirce (morning only)
Commissioner Elad Roisman (morning only)

Advisory Committee Members[1]
Anne Sheehan (Chair)
Elisse Walter (Vice Chair) (by telephone)
Craig Goettsch (Secretary)
Allison Bennington
John Coates
Lisa Fairfax
Rick Fleming
Matthew Furman
Stephen Holmes (by telephone)
Nancy LeaMond
William Lee (by telephone, morning only)
Paul Mahoney (by telephone)
Jennifer Marietta-Westberg
Lydia Mashburn
Mina Nguyen
Barbara Roper (by telephone)
Damon Silvers
Jerome Solomon
Heidi Stam
J.W. Verret
Susan Ferris Wyderko

MORNING SESSION

Welcome Remarks

Chairman Anne Sheehan called the meeting to order shortly after 9:00 a.m.

[1] Anne Simpson was absent.

SEC Chairman Jay Clayton, in his opening remarks, welcomed new Commissioner Roisman, as did the other commissioners who gave opening remarks. Chairman Clayton commented on the two panel discussion topics on the Committee's agenda. He also referred to two statements issued that morning: one by him reiterating that staff views are non-binding, and the other by the Division of Investment Management withdrawing two earlier letters regarding proxy advisory services. Commissioners Peirce, Roisman, and Stein also gave opening remarks, in that order.

Approval of the Minutes of the June 14 Meeting

Following a motion that was made by Mr. Coates and seconded, the Committee voted unanimously to approve the minutes of the previous meeting on June 14, 2018.

Discussion Regarding the U.S. Proxy Voting Infrastructure

Chairman Sheehan introduced the topic and the outside speakers on the two subpanels (both addressing the same topic), who spoke in the following order:

Subpanel One:

- **Ken Bertsch**, Executive Director, Council of Institutional Investors
- **David A. Katz**, Partner, Wachtell, Lipton, Rosen & Katz
- **Brian L. Schorr**, Partner and Chief Legal Officer, Trian Fund Management, L.P.
- **Deborah P. Majoras**, Chief Legal Officer and Secretary, The Procter & Gamble Company
- **Arthur Crozier**, Chairman, Innisfree M&A Incorporated

Subpanel Two:

- **Lyell Dampeer**, President, Investor Communication Solutions U.S., Broadridge Financial Solutions, Inc.
- **Edward Rock**, Martin Lipton Professor of Law; Director, Institute for Corporate Governance & Finance, New York University School of Law (by videoconference)
- **Alexander Lebow**, Co-Founder, SAY

(John Zecca from Nasdaq was unable to attend as scheduled.)

In his opening remarks, Mr. Bertsch noted that the Council of Institutional Investors' asset-owner members seek a proxy voting system that is timely, accurate, transparent (including routine end-to-end vote confirmation) and efficient. He characterized the current system as fraught with inefficiencies with too large a margin for error.

Mr. Katz noted that many shareholders (other than large institutional investors) do not receive proxy voting materials in a timely manner and also that there is no way for an individual shareholder to make sure his or her vote has been accurately and properly cast and counted. He also spoke of issues involving under-voting and over-voting.

Mr. Schorr and Ms. Majoras described specific legal and technical issues that arose in the 2017 proxy contest between Trian and Procter & Gamble and that reportedly frustrated the ability of Procter & Gamble shareholders to access information about the voting process and ensure that their voting instructions were processed accurately. Mr. Schorr and Ms. Majoras found the margin for error in the process especially disconcerting given how close the vote was.

Mr. Crozier explained how discrepancies in the custodial chain of voting authority, which comprises disparate record-keeping systems, can cause problems in counting votes. For instance, when a broker-dealer's clients buy and sell shares, the broker nets the transactions internally and updates the number of shares it holds on an aggregate basis in its ledger account with the Depository Trust Company (DTC), which is a registered clearing agency acting as a securities depository. DTC's nominee, Cede & Co., appears in the corporate issuer's stock records as the sole registered owner of securities deposited at DTC. There is latency in the updating between these intermediaries, which means that at times their record-keeping systems are not reconciled. That in turn can cause the invalidation of otherwise valid votes. Mr. Crozier also remarked on the difficulty of engaging individual shareholders and outlined strategies for increasing their participation.

Messrs. Bertsch, Katz, Schorr and Crozier each expressed support for universal proxy cards, the subject of a 2016 Commission rulemaking proposal.

Professor Ed Rock, who in 2008 published with his colleague Marcel Kahan a seminal article on problems with the U.S. proxy voting infrastructure, outlined what he believes the system requires for its basic legitimacy. A shareholder should be able to know whether or not its vote has been accurately and properly cast and counted, he said; and if there is a problem in the system, the shareholder should be alerted and have an opportunity to fix it. More broadly, Professor Rock asserted that the service-provider market was monopolized, and he suggested that the Commission figure out how to open it to competitive solutions using alternative technologies.

Mr. Lebow acknowledged other participants' optimism with respect to blockchain technology but posed two cautionary questions: first, how would the blockchain be governed, and second, what advantage would blockchain technology have over preexisting database technology. He referred to one of the reform proposals in Professor Rock's article, entailing a restructuring of the system of securities ownership, and suggested that it would be a simpler and more effective solution than blockchain.

Mr. Dampeer sought to clarify that vote reconciliation and confirmation are currently available, albeit not in all cases. He explained that vote reconciliation and confirmation require the cooperation of broker and bank nominees and adherence to a logistical process. He also commented on fees and other issues raised by other speakers.

A discussion with Committee members ensued.

RECESS

The Committee went into recess for lunch and a non-public administrative session at 12:11 p.m.

AFTERNOON SESSION

The meeting resumed at 1:40 p.m. Ms. Sheehan recognized Commissioner Jackson, who had been unable to attend the morning session. He commented on the forthcoming Commission roundtable on the proxy process. Saying that he was troubled by the announcements issued that day, he argued that it would be wrong for the forthcoming SEC roundtable to emphasize politically contentious questions involving regulation of proxy advisory services instead of aiming to fix the voting system.

Discussion Regarding the Commission's Proposed Transaction Fee Pilot in NMS stocks

Mr. Mahoney described a draft recommendation of the Market Structure Subcommittee, and a discussion ensued. Mr. Coates proposed an amendment to strike a reference to the order protection rule and replace it with more general language stating that it would be useful to conduct a broader study of the effects of Regulation NMS.[2] His aim, he explained, was to avoid any perception that the recommendation was an attack on the order protection rule.

A motion was made and seconded to vote on the proposed recommendation with Mr. Coates' amendment. The motion was passed, with all but two of the members who were present voting in favor of the recommendation. Mr. Furman abstained, and Ms. Mashburn voted against the motion.[3]

Discussion Regarding the Implications of Passive Investing

Mr. Coates introduced the topic and the panel members, who spoke in the following order:

- **Jeb B. Doggett,** Managing Director, Casey Quirk by Deloitte
- **Rodney Comegys,** Head, Equity Indexing Group, Vanguard
- **Robert W. Sharps,** Group Chief Investment Officer, T. Rowe Price Group, Inc.
- **Marcel Kahan,** George T. Lowry Professor of Law, New York University School of Law Law (by videoconference)
- **Robert C. Pozen,** Senior Lecturer, MIT Sloan School of Management

[2] Specifically, the amendment was to strike the following two sentences from the penultimate paragraph of the recommendation that stated, "It would be useful to consider whether aspects of the regulation, including the order protection rule, have led exchanges, broker-dealers, and market professionals to act in ways that were unanticipated and may not be in the best interests of investors. If so, midcourse corrections to the regulation may be in order." [Footnote omitted.] In lieu of the stricken text, the amendment would insert the following sentence: "It would be useful to conduct a broader study of the effects of Regulation NMS with a view to other possible reforms."

[3] It appeared that Ms. Mashburn may have voted in favor of the recommendation, but she explained afterward that she had intended to vote against it.

Mr. Doggett gave an overview of trends in passive investing, including its size, market demand and sources of growth. He also offered a forecast of the market in five years.

Mr. Comegys described the benefits of passive investing to retail investors, including the advantages of lower fees. In addition, he disputed the idea that passive investing causes either market bubbles or volatility.

Mr. Sharps, offering the perspective of an active investor, described what he called observable impacts of passive investing on market structure, price discovery, and corporate governance. He cited examples of heightened correlations of index constituents and increasing concentration of late-day trading.

Mr. Kahan addressed questions of whether the growth of passive investing had an impact on market pricing, market efficiency, and corporate governance. He argued that market efficiency had not been affected because the growth in indexing had come largely from retail investors rather than from investment professionals.

Mr. Pozen made six points about passive investing, ranging from price discovery to proxy voting, from ESG investment considerations to the purchase of IPOs. Echoing remarks by Mr. Sharps and Mr. Kahan, Mr. Pozen cautioned against any policy making that would favor passive over active investing.

A discussion with Committee members ensued.

Subcommittee Reports

Mr. Furman and Mr. Coates offered brief updates, respectively, of the work of Market Structure Subcommittee and Investor as Owner Subcommittee. Ms. Sheehan touched on the work of the Investor as Purchaser Subcommittee and described plans for the December 13 public meeting.

CLOSING

Chairman Sheehan adjourned the meeting at 3:38 p.m.