

### 5.3. Specific request for comment

We specifically seek comments in response to the following questions from *all market participants*:

#### *General*

1. Do you agree, or disagree, with each of the concerns identified in the Consultation Paper, namely: (i) potential conflicts of interest, (ii) perceived lack of transparency, (iii) potential inaccuracies and limited engagement with issuers, (iv) potential inappropriate influence on corporate governance practices, and (v) the extent of reliance by institutional investors on the advice of such firms? Please explain and, if you disagree, please provide specific reasons for your position.

Response (i): We agree that there is presence of potential conflict of interests inherent in this industry. To reduce such potential conflicts of interests, the companies should have specific policies requiring them to disclose their investments and/ or all affiliations of the advisory company, its directors, founders, shareholders and senior employees with any company along with specific disclosures in its advisory reports detailing the potential conflict issues or relationships. Further, the company should have Chinese walls to separate the division facing issuer and the division facing client. Such Chinese walls should completely block information flows. Additionally the firms should disclose to all clients and potential clients in clear words the conflict of interests of the firm as well as senior management and disclose the same on website, which should be updated periodically.

Response (ii): We agree with the perceived lack of transparency in the industry. A way forward for the industry would be to disclose its policies governing the analysis related to resolutions & provide guiding laws/ regulations/ rules/ recommendations from where they have been deduced. This will not only bring transparency but also rule out to large extent inconsistent analysis

Response (iii): We do not agree that potential inaccuracies in relation to proxy advisory firms alone should be a cause of concern. Accuracy/inaccuracy is part of any business or system. Each organization is aware of the same and its impact on the reputation and credibility of the organization. Inconsistencies and inaccuracies



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will hurt business interest of these firms more than that of anyone else. Whether internal systems and procedures are robust enough to minimize such instances should be the headache of proxy advisory firms, unless the same are intentional. Furthermore, factual inaccuracies and wrong analysis would destroy the credibility of the company in market and every company would strive to reduce any such errors on their part. Further transparent systems/guidelines will also enable feedback from issuers/users to rectify mistakes.

However, there can be instances of wrong interpretations of certain resolutions / explanations which can lead to a wrong conclusion and therefore the companies should engage with issuers. But on the flip side, there is a potential for leak of proxy report by the company insiders and / or delay in responding to the proxy firms. Therefore, if any regulation is to be brought about such engagements, it should come with an additional regulation on the part of issuers to respond within a given duration.

Response (iv): We do not agree with the concern that there could be a situation which could cause potential inappropriate influence on corporate governance practices. This presupposes that either the Proxy advisory firms use arm twisting methods or the corporates are not rational enough and would follow what is inappropriate for them from the business point of view. We are of the opinion that shareholders using services of proxy advisory firms debate on the issues in general meetings and if management comes out with reasonable answers, they need not insist. In fact a feedback system of what happened in the meeting, how the resolutions were voted in the meetings and which of the recommendation of proxy firm were accepted/not accepted will help both the issuers as well as firms to revise their systems and avoid unreasonable fear of inappropriate influence. Further, if the Proxy Advisors disclose their policies and guidelines from where they deduce their policies, the scope for inappropriate influence will be reduced.

Response (v): We do not agree with the concern because of two reasons. One, institutional investors are sophisticated investors and are capable of taking their own decisions. The reason they usually use service is economics of using proxy advisors as cost of such analysis is shared by all users. Such investors usually have guidelines on voting and they normally stick to them. However, they may consult the proxy advisory report for taking final decisions. As detailed previously, if the guidelines which govern proxy policy are transparent with explanations for



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rationale behind each of the guideline inappropriate influence is not possible. Additionally, as the industry grows more and more firms will enter into the market and gradually the institutional investors will seek out more than 1 proxy advisory firm to advise them on important resolutions. Accordingly, if concern (ii) has been taken care of they can weigh factors taken into account from all such advisory firms and arrive at their independent conclusion. We have to understand that these are institutional investors and they already have the expertise, resource and knowledge to analyze any conflicting advice from two or more proxy advisory firms.

2. Are there other material concerns with proxy advisory firms that have not been identified? Please explain.

Response: The recommendations of Proxy Advisory firms for special resolutions such as M&A, may potentially affect the markets and therefore it is impertinent to have policies and guidelines wherein the team working on such resolutions are prohibited to act or cause to act on the news prior to public dissemination. Secondly, these proxy advisory firms are also in a business and have motivation to make profits. Such motives may cause the proxy advisory firms to sensationalize the recommendations to market them, which may cause adverse market movements. Similarly, partners or senior management sitting on board of proxy advisory firms may have affiliations or may be a board member of other public companies. Such associations may reflect as favorable recommendation for such public companies.

3. Are there specific gaps in the current practices of proxy advisory firms which justify regulatory intervention? Is there a concern that future gaps could be created as a result of new entrants or changes in business or other practices?

Response: Setting transparency and disclosure standards will take care of all the concerns/potential concerns.

4. Do you believe that the activities of proxy advisory firms should be regulated in some respects and, if so, why and how?

Response: No, We believe self regulation is the best form of regulation for such firms, activities of proxy advisory firms should be treated as the activities of a consultancy firm. We believe that credibility, absence of conflicts, transparency

and independence are pillars on which proxy advisory firms' reputation stands. The question how strong these pillars are would vary from one firm to another. However there could be regulatory guidelines as opposed to regulations. These guidelines could define benchmark against which issuers/investors can evaluate these firms. The guidelines could also define the scope of their activities. Such firms should have zero conflict of interest situation and should abide by comply or explain policies if they cannot avoid such situations. Further, these firms should on quarterly intervals declare their independence on their websites.

### ***Potential conflicts of interest***

5. To what extent do you consider proxy advisory firms to: (i) be subject to conflicts of interest in practice, (ii) already have in place appropriate conflict mitigation measures, and (iii) be sufficiently transparent regarding the potential conflicts of interests they may face? If you are of the view that current disclosure by proxy advisory firms regarding potential conflicts of interest is not sufficient, please provide specific examples of such insufficient conflicts of interest disclosure and suggestions as to how such disclosure could be improved.

Response:

- (i) As detailed elsewhere we are of the opinion that firms may have conflict of interest in practice
- (ii) Each firm has appropriate conflict mitigation measures in place, however whether the same are sufficient or not will remain subjective till such time a bench mark is set
- (iii) At no point of time one can say that a firm is sufficiently transparent regarding the potential conflicts of interests they may face as not all possible conflict situations could be envisaged, sufficiency can only be far known or potentially known conflict situations.

Current disclosures in our opinion examine relationship up-to one level e.g. Say A is a responsible person in the advisory firm and he is associated with a company X. In company X he has fellow directors B, C, and D. The question is whether potential conflict of interest situation is limited to company A only or it extends to all such companies where B, C, or D are associated in any capacity? Also, whether we should stop at two levels or move to third level as well? There are no hard and fast answers. Ideally, to avoid such situations, the firm and its employees including directors should have no association with any issuer. Our company SES operates on this principle.

6. If you are of the view that there are conflicts of interest within proxy advisory firms that have not been appropriately mitigated, which of these are the most serious in terms of the potential (negative) impact on development of their voting recommendations and why?

Response: Same as in 5(iii) above

7. Should we propose an amendment to NI 51-102 to require reporting issuers to disclose consulting services from proxy advisors in their proxy circular? Or would such disclosure undermine the existing controls and procedures (i.e., “ethical wall”) in place which currently may prevent proxy advisory firm research staff who review an issuer’s disclosure from being made aware of the identity of their firm’s consulting clients?

We do not question the effectiveness of Chinese walls but they are also not fool proof solutions to prevent information spill over. One division may not know the confidential names in list of another division. However gatherings and employee socializing activities are common ground for discussing sensitive information. In our opinion, material non-public information is highly dangerous and therefore, we feel that full transparency is must.

### ***Perceived lack of transparency***

8. Could disclosure of underlying methodologies and analysis provide beneficial information to the market or would the commercial costs of doing so be too significant?

Response: In our opinion disclosure of underlying methodologies and analysis will provide beneficial information to the market and is a must. While there will be no financial cost for the same however it could have commercial cost as competitors might copy the same. A balance has to be kept between disclosure and commercial interest.

### ***Issuer engagement***

9. To what extent could there be an improvement in the dialogue with issuers during the vote recommendation process?

Response: There can be substantial improvement in the engagement. If the Proxy Advisory firm has disclosed its policies for evaluating resolutions, the issuers while reviewing the reports can highlight any factual error or misunderstanding of



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certain facts. However, there will have to be strict regulations to monitor the confidentiality agreement

10. During proxy season, is it appropriate for a proxy advisory firm to engage with issuers in all circumstances or are there legitimate business and policy reasons why it should not be required to do so? Are there certain special types of situations where it is more important that issuers are able to engage with proxy advisory firms?

Response: For standard resolutions, the proxy advisory firms need not engage with the issuers, however for special and unique resolutions the firms can engage with the issuers to deliberate upon the facts. The issuers should also be given a fair chance to present their case and the firms should take cognizance of their requests while advocating final recommendation, however, timelines are very important during proxy season and in no case confidentiality should be breached. Any leakage of the contents of report from issuers end might hurt commercial interests of the proxy advisor.

11. If a proxy advisory firm, as a matter of policy, believes that there are certain circumstances where it is not appropriate for it to give issuers an opportunity to review its reports, would it be sufficient to only require in these circumstances that the underlying rationale for such policy be disclosed? Please explain. Or, alternatively should proxy advisory firms be required to provide issuers with an opportunity to review their reports in all circumstances?

Response: As stated in #10 above, we do not feel that there could be any issue which cannot be discussed with the issuer. However we strongly feel that sensitivity of timelines along with confidentiality and commercial concerns could be the limiting factors for engagement. On the other hand, we feel that only when the advisory firm is deviating from its stated policy/guidelines and rationale in respect of any advisory engagement must be must.

12. Should we prescribe the details of the processes that proxy advisory firms implement to engage with issuers? If so, what do you suggest the requirements should be?

Response: No.

### ***Potentially inappropriate influence on corporate governance practices***

13. To what extent should there be a more fair and transparent dialogue between proxy advisors and market participants on the development of voting policies and guidelines? Is it sufficient for proxy advisors to address governance matters by soliciting comments from their clients?

Response: Policy formulation should be a holistic process. The proxy advisory firms should engage clients as well as issuers to discuss and deliberate upon its policies. However, it should also constitute an independent and knowledgeable advisory committee of its own to incorporate the suggestions. Further, the proxy advisory firms should also do an impact analysis of its significant recommendations and create a database for all such recommendations. Every five years, there should be a retrospective analysis of such recommendations and an analysis should be done to understand the impact if an opposite recommendation was issued versus its current impact. Further the policies should not be cast in stone and should take a note of changes as and when they happen. Any deviation from stated policy should be noted and duly explained in the report along with rationale. We believe that tick box approach advisory should not be adhered to.

***Proposed regulatory responses and framework(s)***

14. Do you think a securities regulatory response is warranted in connection with each of the concerns identified above? Please explain why or why not.

15. Do you agree with the suggested securities regulatory responses to each of the concerns raised? If not, what alternatives would you suggest?

16. Do you agree or disagree with the requirements and disclosure framework set out in section 5.2.1 to address the concerns identified? If not, please indicate why. Would you prefer instead one of the other suggested securities regulatory frameworks identified above? If so, please indicate why. Do you agree or disagree with our analysis of these frameworks? Do you have suggestions for an alternative regulatory framework?

17. Are you of the view that we should prescribe requirements in addition to or instead of those identified above for proxy advisory firms?

Response to 14-17: As detailed elsewhere we feel that rather than regulation, voluntary guidelines should be issued by the regulator rather than detailed



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regulation and need for registration. Further, it should be included in the guideline that the advisory firms should disclose their compliance (voluntary) with the guidelines. Compliance with voluntary guidelines would be a distinguishing factor for establishing credibility of the firm.

**Additional questions for *institutional investors*:**

18. To what extent and in what ways do you rely on the services provided by proxy advisory firms? Please be as specific as possible.

19. How do you view your duty to vote and how do the vote recommendations of proxy advisory firms play a part in your decision-making process?

20. Do institutional investors have the ability to require changes to proxy advisory firms' practices without the need for regulatory intervention?

21. Assuming you share the concerns identified above, do lack of choice/competition or other market factors in the proxy advisory industry limit your ability to address these concerns directly such that regulatory intervention is warranted? Please explain.

22. Given the above-noted concerns regarding the overall quality and lack of transparency underlying the vote recommendations of proxy advisory firms, what measures do you take and, overall, how do you gain assurance that such recommendations are reliable for your voting purposes?

23. Do you view the policy development process and resulting proxy voting guidelines of proxy advisory firms as appropriate and reflective of your governance preferences and views? Would input from issuers further benefit or potentially hinder such process?

**Additional questions for *issuers*:**

24. Overall, what has been your experience with proxy advisory firms? Please be as specific as possible.

25. Do you believe that the concerns identified negatively affect voting outcomes at shareholders' meetings? Please provide specific examples of situations where



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any of the concerns identified above resulted in what you consider to be an inappropriate vote outcome and describe the nature and extent of the harm caused to market integrity.

26. To what extent do you adopt the corporate governance standards proposed by proxy advisory firms in your choice of corporate governance policies, even if such standards are not appropriate for your organization? Please provide examples of the types of practices that have been changed due to a proxy advisory firm's guidelines and why such changes were not appropriate or did not improve your organization's overall corporate governance.

27. In those instances where you have identified potential inaccuracies in a proxy advisory firm's recommendation, were these material inaccuracies that would have resulted in a change in the proxy advisory firm's vote recommendation? Please provide specific examples of how this situation resulted in an improper vote outcome (i.e., what was the risk to market integrity).

**Additional questions for *proxy advisory firms*:**

28. What are your views with respect to the concerns identified and with any of the possible regulatory approaches to these concerns?

Response: Our response to previous question adequately reflect our views

29. In connection with the possible regulatory approaches, do you have concerns about disclosure of confidential or proprietary information? Please explain.

Response: Yes, regulations on disclosing confidential / proprietary information without adequate provisions to prevent mushrooming of proxy advisory firms may affect the perception of credibility from such proxy advisory firms.

30. What impact could the preferred securities regulatory framework (requirements and disclosure) have on your operations? Please provide details and, where appropriate, propose an alternate approach.

Response: Our firm is based out of India and is still in its nascent stage as is the market for such services here. Understandably, there are neither any guidelines nor any regulations governing our activities. However, as the principal founder of our firm has been an ex-regulator himself and has been active in advocating full disclosures and maintaining zero conflict of interest, we have voluntarily made full



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disclosures and have avoided any conflict of interest in our firm. Further, we have set up the organization with a not for profit motivation and none of the manager/directors of the firm are on board of any public companies.

31. In addition to your responses to the questions posed, we also welcome any additional information and data you can provide to inform our continued review and analysis of the issues identified in the Consultation Paper.