IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

INSTITUTIONAL SHAREHOLDER SERVICES INC.,

Plaintiff,

v.

SECURITIES AND EXCHANGE COMMISSION and WALTER CLAYTON III in his official capacity as Chairman of the Securities and Exchange Commission,

Defendants.

Case No. 1:19-cv-3275-APM

REPLY IN SUPPORT OF INTERVENOR THE NATIONAL ASSOCIATION OF MANUFACTURERS' CROSS-MOTION FOR SUMMARY JUDGMENT

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December 9, 2020

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INTRODUCTION

In 1991, ISS proclaimed that "ISS believes that informed voting decisionmaking will be facilitated if an issuer's response to its proxy analyses and voting advice can be incorporated into its products. Securityholders will then have the dual benefit of ISS's objective analysis and advice coupled with the issuer's critique thereof."[1] The Final Rules directly advance this goal, and ISS's brief confirms that the modest regulatory reforms that the Securities and Exchange Commission promulgated to bring much-needed transparency and accuracy to the market for shareholder proxy voting advice easily satisfy the Administrative Procedure Act. The Finals Rules are well within the Commission's statutory authority to regulate the "solicit[ation]" of any proxy, are directed to a well-documented market problem, and are consistent with the First Amendment.

ISS does not dispute that when the Exchange Act was enacted, the word "solicit" ordinarily meant both (1) to "endeavor to obtain" an action, and (2) to "awake or excite to action." That concession should end any question concerning the SEC's statutory authority. When a firm encourages shareholders to hire it for its proxy voting advice and advises those shareholders on how they should vote their shares in connection with particular ballot measures, there can be no serious question that the firm has "solicited" a proxy under the ordinary meaning of the term. That common-sense conclusion is particularly obvious where the firm automatically submits its clients' votes in line with its recommendations, as ISS does. ISS clearly is urging its clients to vote their shares in a particular way, and thus is soliciting their proxy. This is precisely the situation that Congress authorized the Commission to regulate in enacting Section 14(a).

The Final Rules' carefully calibrated effort to oversee these solicitations without imposing

[1] Ltr. from ISS to SEC re Exchange Act Release No. 29315, at 3 (Aug. 1, 1991) (emphasis added). A copy of this publicly filed letter is attached for the Court's convenience as Exhibit A.

undue burdens is eminently reasonable, and ISS does not come within a country mile of showing otherwise. For forty years, the Commission's proxy regulations have made clear that to render proxy voting advice is to solicit a proxy. The Commission, therefore, could have subjected all proxy voting advice to the general regulatory framework applicable to proxy solicitations. It did not do so. Instead, the Commission offered firms like ISS an exemption from the normal filing and information requirements applicable to proxy solicitations if the firms meet basic disclosure requirements—all in line with other disclosures required in our nation's securities laws.

The goal of these reforms was straightforward: By incentivizing proxy voting advice businesses to issue more thorough disclosures, the Final Rules sought to improve the total mix of information available to shareholders. That is a laudable goal and a perfectly reasonable, balanced response to mounting criticism that the market for proxy voting advice is beset with errors and undisclosed conflicts of interest.

ARGUMENT

The Final Rules and the Proxy Guidance do not exceed the Commission's statutory authority, are not arbitrary and capricious, and do not violate the First Amendment.

I. ISS's Strained Interpretation Of "Solicit" Is Unavailing.

Section 14(a) of the Exchange Act grants the Commission broad authority to regulate "*any* person" who "solicit[s] *any* proxy ... in respect of *any* security." 15 U.S.C. § 78n(a)(1) (emphases added). ISS's opposition confirms that "proxy voting advice" is a form of "solicitation" lawfully subject to SEC regulation.

A. ISS's Arguments For Evading The Plain Text Of The Exchange Act Fail.

ISS does not dispute that when the Exchange Act was enacted, the word "solicit" ordinarily meant both (1) to "endeavor to obtain" an action, and (2) to "awake or excite to action." Black's Law Dictionary 1639 (3d ed. 1933); *see* ISS Reply 14; *see also* NAM SJ Mem. 13; SEC SJ Mem.

22; Business Organizations Amicus Br. 7 (Dkt. 43). In providing proxy voting advice to their clients, ISS and other proxy voting advice businesses easily satisfy these definitions.

1. Contrary to ISS's assertion (at 3), a proxy voting advice business "endeavors to obtain" a vote in line with its recommendation. ISS does not dispute that it encourages clients to hire it for its advice with the expectation that the advice will drive the client's voting decision. *See* ISS Reply 4 n.1; ISS SJ Mem. 19. As part of that advice, it tells the client exactly how to vote its shares in connection with particular ballot measures. *See* ISS Reply 3. Further, in many cases, ISS automatically submits clients' votes in line with its own recommendations. *Id.* at 15; *see Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice*, 84 Fed. Reg. 66,518, 66,520 (Dec. 4, 2019) (noting that clients can have pre-populated ballots "submitted automatically, without further client review"). That is soliciting a proxy by any definition. *See* NAM SJ Mem. 13–14; Business Organizations Amicus Br. 8–9.

In stark contrast to Section 14(a)'s expansive language, ISS argues for a restricted, idiosyncratic definition of the term "solicit" that has no basis in the statute or the English language. By ISS's telling, "solicit" covers only those instances in which a person subjectively hopes to obtain "a certain outcome" in the overall ballot measure. ISS Reply 1. There is no evidence that Congress sought to condition the Commission's Section 14(a) authority on such fine questions of subjective intent. Nor is there any reason to suppose that the "intent," if it were relevant, must be to influence the outcome of the overall ballot measure, rather than the outcome of the individual shareholder's vote. ISS offers no responses to these glaring problems with its preferred definition.

Even if intent to influence the outcome of the ballot measure were relevant, the Commission credited significant evidence that proxy voting advice businesses often *do* "have an interest in the outcome of matters being voted upon at shareholder meetings" and *do* "seek proxy authority

for themselves." *Exemptions from the Proxy Rules for Proxy Voting Advice*, 85 Fed. Reg. 55,082, 55,093 n.141 (Sept. 3, 2020). There is no dispute that ISS "operates a consulting business that counsels companies on the very corporate governance policies on which the advisory side of the firm makes recommendations." AR585 at 4; *see* 85 Fed. Reg. at 55,126. ISS, moreover, like other proxy voting advice businesses, advises on matters on which the firm or its affiliates have a preference and "want to have a positive influence." 85 Fed. Reg. at 55,093 n.141 (quoting U.S. Gov't Accountability Off., GAO–17–47, *Corporate Shareholder Meetings: Proxy Advisory Firms' Role in Voting and Corporate Governance Practices* 18 (2016) ("GAO Report")); *see also* AR558 at 11. The Commission's findings on these points are "supported by 'substantial evidence'" and conclusive even under ISS's crabbed and atextual definition. *Nat'l Rural Elec. Co-op. Ass'n v. SEC*, 276 F.3d 609, 614 (D.C. Cir. 2002).

ISS's practice of "robo-voting" its clients' shares underscores that it is engaged in solicitation. *See* NAM SJ Mem. 14; *see also* Business Organizations Amicus Br. 8–9. ISS does not deny that when it automatically submits its clients' votes in line with its own recommendations, it has endeavored to obtain those clients' proxies—and successfully so. ISS Reply 15. That ISS claims to have built safeguards into its robo-voting platform, *see id.*, does not alter the essential character of ISS's actions. These actions show that ISS is soliciting proxies, even on its own understanding of the term, because it is seeking and indeed actually obtaining "a certain outcome." ISS Reply 1.

ISS attempts to deflect scrutiny of its practice of automatically submitting client votes by invoking the *Chenery* doctrine and arguing that the Commission supposedly "*rejected*" requests to "regulate electronic proxy voting platforms." ISS Reply 15; *see SEC v. Chenery Corp.*, 318 U.S. 80, 93–95 (1943). ISS is wrong on numerous levels. Foremost, the NAM is not suggesting that the Final Rules impose limits on robo-voting platforms, but is merely showing one of the ways

in which ISS *does* seek outcomes, and therefore engages in "solicitation" even under its own preferred definition. That is, the NAM is not challenging the Commission's decision not to adopt such regulation at this time;[2] it is arguing in support of the agency's interpretation of "solicit." And legal arguments about the "interpretation of [a statute]" do not implicate *Chenery*, *Sierra Club v. FERC*, 827 F.3d 36, 49 (D.C. Cir. 2016), least of all when "the agency has come to a conclusion to which it was bound to come as a matter of law," *United Video, Inc. v. FCC*, 890 F.2d 1173, 1190 (D.C. Cir. 1989). Nor does *Chenery* bar the NAM from impeaching ISS's claim to be a neutral dispenser of objective advice with evidence from the administrative record showing that ISS is in fact an active promoter of outcomes. *Cf. Chiquita Brands Int'l, Inc. v. SEC*, 805 F.3d 289, 299 (D.C. Cir. 2015) (*Chenery* does not bar counsel from "elaborating" on an interpretation).

In any event, while the term "solicit" undoubtedly encompasses efforts to achieve a particular outcome in the ballot measure, it is in no way limited to that situation. *See* NAM SJ Mem. 20. The word "outcome" does not appear in the statute, which addresses "*any* proxy"—in the singular—not the tally of *all* proxies. *See* 15 U.S.C. § 78n. Endeavoring to obtain an individual client's proxy is no less a solicitation than endeavoring to obtain a particular outcome in the vote.

Similarly, the "risk of abuse" in proxy solicitation that ISS claims Congress sought to regulate, ISS SJ Mem. 4, is equally present when a firm seeks to obtain an individual proxy vote as opposed to an overall outcome. ISS surely intends for its paying clients to follow its advice, as evidenced by its professed concerns over the alleged dilution of its proxy-voting "viewpoint." *See* ISS Reply 2, 33, 36, 37, 39, 43. This is true even when ISS "offers different recommendations

[2] Regardless, the Commission merely "declined to adopt such a prescriptive approach *at this time*" while *confirming* that it "could require such a condition." 85 Fed. Reg. at 55,144 (emphasis added). The Commission's statements therefore show that the regulation of robo-voting platforms falls comfortably within its Section 14(a) authority.

about the same matter" to different clients. *See* ISS Reply 3, 4, 13. At a minimum, ISS seeks to persuade each client to vote in line with ISS's individual recommendations. Likewise, if ISS has a duty to act in the "best interests of its clients," ISS Reply 28, it must *try* to convince each client to vote as ISS thinks is best. As "[o]fficials from one proxy advisory firm" reported, "they *want*" to "influence" their clients because it is "part of their responsibility" to "promote good governance" (as they see it). 85 Fed. Reg. at 55,093 n.141 (emphasis added) (quoting GAO Report 18). In short, they solicit their clients' proxies, whether in individual cases or in the aggregate.

2. In addition to endeavoring to obtain an outcome, proxy voting advice businesses also engage in activities that "awake or excite to action." Black's Law Dictionary 1639. ISS concedes that this, too, is a permissible definition of "solicit." ISS Reply 3, 14. In light of ISS's further admission that there "is no question that a proxy adviser's recommendations might 'influence' the decisions of the investor-client," ISS SJ Mem. 19, there can be no question that ISS satisfies this definition of "solicit." To be sure, ISS notes that *other* definitions of "solicit" were listed as "rare" in a single dictionary in 1934, ISS Reply 4 (quoting Webster's New International Dictionary (2d ed. 1934)), but that fails to answer why ISS's proxy voting advice does not "awake or excite to action" the voting of its clients' proxies.

ISS's argument that the solicitor "must still have a specific *objective* or *outcome*" in mind, ISS Reply 4, does not change this plain meaning of "solicit." The definition "awake or excite to action" requires no subjective intent at all. As the term was understood in 1934, even an inanimate object could "solici[t]" someone insofar as it "serve[d] as a temptation or lure" to act. Webster's New International Dictionary 2394. ISS's proxy voting advice easily meets that definition.

B. ISS Fails To Account For The Structure And History Of The Exchange Act.

Contrary to ISS's arguments, the structure and history of the Exchange Act confirm that proxy voting advice is a form of solicitation.

1. ISS ignores the regulatory history. As the NAM explained in its opening brief (at 16–17), by the 1970s, there was no question that the Commission's administrative interpretation of "solicit" included proxy voting advice. In 1979, for example, the Commission specifically exempted, through notice-and-comment rulemaking, the "furnishing of [certain] proxy voting advice" from various regulatory requirements applicable to solicitations—necessarily presupposing that proxy voting advice was a form of solicitation. *Shareholder Communications, Shareholder Participation in the Corporate Electoral Process and Corporate Governance Generally*, 44 Fed. Reg. 68,764, 68,769–70 (Nov. 29, 1979); *see infra* pp. 16–19 (detailing this history).

Against this backdrop, Congress's amendments to Section 14 strongly support the Commission's interpretation. By "revisit[ing] [this] statute" in later years "without pertinent change," Congress indicated that the Commission's longstanding interpretation was "the one intended by Congress." *CFTC v. Schor*, 478 U.S. 833, 846 (1986); *see* NAM SJ Mem. 16. This is not a case, as ISS argues (at 16), where Congress's failure to override the agency's interpretation could plausibly flow from "unawareness, preoccupation, or paralysis." *Citizens for Responsibility & Ethics in Washington v. FEC*, 316 F. Supp. 3d 349, 410 n.47 (D.D.C. 2018), *aff'd*, 971 F.3d 340 (D.C. Cir. 2020). Rather, "Congress's inaction for over forty years" is "particularly significant" here because it has "amended various parts of the [Exchange Act] over the years, *including the specific provision at issue here.*" *Jackson v. Modly*, 949 F.3d 763, 773 (D.C. Cir. 2020) (emphasis added); *see* 15 U.S.C. § 78n; Pub. L. No. 111-203, § 953, 124 Stat. 1376, 1903 (2010) (adding subsection on "proxy" "solicitation"); Pub. L. No. 98-38, § 2, 97 Stat. 205, 205 (1983) (same). Yet, Congress "has never sought to override" the Commission's determination that proxy voting advice is a form of solicitation. *Jackson*, 949 F.3d at 773. "These circumstances provide further evidence—if more

[were] needed—that Congress intended the Agency's interpretation, or at least understood the interpretation as statutorily permissible." *Barnhart v. Walton*, 535 U.S. 212, 220 (2002).

Congress also ratified the Commission's interpretation of the phrase "solicit any proxy" by later reenacting that same language in another provision of Section 14. *See* NAM SJ Mem. 17–19; *see also* Pub. L. No. 103-202, § 302, 107 Stat. 2344, 2359 (1993) (codified at 15 U.S.C. § 78n(h)(1)). ISS quibbles (at 17) that there is no evidence that "Congress was contemplating proxy voting advice" when it reenacted the same language in 1993. Yet, Congress borrowed wholesale the phrase "solicit any proxy," and it is implausible that Congress would have done so without understanding the settled construction of that phrase. "Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when," as here, it re-enacts statutory language without change. *Lamar, Archer & Cofrin, LLP v. Appling*, 138 S. Ct. 1752, 1762 (2018); *see also Bragdon v. Abbott*, 524 U.S. 624, 645 (1998) ("When administrative and judicial interpretations have settled the meaning of an existing statutory provision, repetition of the same language in a new statute indicates, as a general matter, the intent to incorporate its administrative and judicial interpretations as well.").

2. ISS also ignores or misreads the statutory context, which further confirms that proxy voting advice is a form of solicitation.

a. ISS correctly observes (at 8) that a statutory reading generally should be rejected where Congress "could easily have chosen clearer language" to achieve the asserted result. *NLRB v. SW Gen., Inc.*, 137 S. Ct. 929, 939 (2017). That principle resolves this case—although not in the way ISS suggests. *See* NAM SJ Mem. 21. Here, if Congress really sought to limit the reach of the statute to those with a "predetermined *objective* or *outcome*" in mind, ISS Reply 1, it easily could have addressed the solicitation of a proxy "for the purpose of inducing" a vote—a formulation

already appearing in Section 9(a)(2) of the Act. Pub. L. No. 73-290, § 9(a)(2), 48 Stat. 881, 889 (1934). Similarly, if Congress had sought to reach only those "unscrupulous corporate officials seeking to retain control of the management" of the corporation, ISS Reply 11 (quoting S. Rep. No. 73-1455, at 77 (1934)), it could have targeted "[s]oliciting of proxies *by an agent of the company ... for use of officers of the company*," *State ex rel. Pugh v. Meredith*, 167 N.W. 626, 627 (Iowa 1918) (emphasis added), as other statutes of the day did, thus limiting the prohibition to certain actors with certain purposes.

ISS's alternative formulation (at 8) does not move the needle. Congress *could* have spoken of communications made "in connection with" a proxy vote, but it is doubtful that would have been "clearer." ISS Reply 8. The ordinary meaning of "solicit" as including "to awake or excite to action" already encompassed action that would "*influence* a proxy vote," *id.*, so ISS's alternative formulation would only serve to raise difficult questions of overbreadth. Suppose a corporation made false statements to a state regulator about the outcome of a proxy vote. Those statements would be made "in connection with" a proxy vote, but they would not be the solicitation of a proxy. Congress sought to authorize the regulation of solicitation, not any conceivable communication concerning a proxy vote.

b. ISS (at 17) also misunderstands other unchallenged portions of the Final Rules, which would make little sense under ISS's interpretation. *See* NAM SJ Mem. 21–22. For example, most "shareholders own their securities in 'street name,'" meaning a broker-dealer holds the securities in its own name on behalf of its customers. 85 Fed. Reg. at 55,094. In that situation, broker-dealers must "forward a company's proxy materials to their customers." *Id.* But what if a broker-dealer "transmit[s] some but not all proxy solicitations"? *Walsh & Levine v. Peoria & E. Ry. Co.*, 222 F. Supp. 516, 519 (S.D.N.Y. 1963). If ISS is right—that is, if the definition of solicitation

reaches only those communications that seek a particular objective—neither the aggrieved customer nor the Commission would have any recourse under Section 14, as the broker-dealers "have no interest in the outcome of the matters being presented for a vote." 85 Fed. Reg. at 55,094. But that is not how the regulations work. Because forwarding proxy materials *is* "treated as [a] solicitation[ ] under the proxy rules," *id.*, a broker-dealer's failure to forward all of the materials would potentially subject it to liability under Section 14(a), *see Walsh & Levine*, 222 F. Supp. at 519 (broker-dealer must "fulfill the duties required of active proxy solicitors").

II. ISS Fails To Show That The Final Rules Are Arbitrary And Capricious.

ISS continues to "quibble with the Commission's policy choices," but it is not the role of this Court, nor that of ISS, to "'substitute [its] judgment for that of the agency.'" *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 530 (2009) (quoting *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983)); *see also Bradford Nat'l Clearing Corp. v. SEC*, 590 F.2d 1085, 1114 n.46 (D.C. Cir. 1978). Quite the opposite: The "scope of review" under the Administrative Procedure Act's "'arbitrary and capricious' standard is narrow." *State Farm*, 463 U.S. at 43. ISS has not identified any "relevant factors" that the Commission failed to consider. *Id.* at 42. Nor has it identified any decision by the SEC that "runs counter to the evidence before the agency." *Id.* at 43. The Final Rules are "reasonable and must be upheld." *Small Refiner Lead Phase-Down Task Force v. EPA*, 705 F.2d 506, 521 (D.C. Cir. 1983).

A. The Commission Reasonably Explained The Policy Concerns Justifying The Final Rules.

1. ISS repeatedly asserts (at 1, 17–21) that the Commission has not identified a "problem" that the Final Rules are needed to solve. But repetition does not make it true.

The Final Rules are the culmination of a long, well-documented administrative record in which interested parties engaged the Commission over many years about the need for oversight of

proxy voting advice businesses. As ISS and other "proxy voting advice businesses have become an increasingly important and prominent part of the proxy voting process," "registrants, investors, and others have expressed" growing concerns. 85 Fed. Reg. at 55,085. "These concerns include the accuracy and soundness of the information, and the transparency of the methodologies, used to formulate proxy voting advice businesses' recommendations." *Id.*; *see also id.* at 55,102, 55,103 & nn.253–58, 55,106 & nn.303–04; NAM SJ Mem. 7–8, 23; Business Organizations Amicus Br. 13–16. "Concerns have also focused on potential conflicts of interest that may affect the recommendations made by the proxy voting advice businesses." 85 Fed. Reg. at 55,085; *see also id.* at 55,097 nn.193–94; NAM SJ Mem. 7, 23; Business Organizations Amicus Br. 10–13. These and other "concerns … prompted the Commission to consider" the Final Rules, 85 Fed. Reg. at 55,085, and thoroughly belie ISS's claim that there is no "problem" for those rules to address.

ISS argues (at 18) that the Commission cannot justify the Final Rules because those rules were supposedly "broadly opposed by every segment of the investment community." That is false, *see*, *e.g.*, 85 Fed. Reg. 55,089 & nn. 85–86, but even if it were true, it would be irrelevant. The Commission is not limited to promulgating only rules favored by the "well-resourced, experienced, and sophisticated entities" that ISS serves. ISS Reply 21. By statute, the Commission regulates for the broader "public interest," 15 U.S.C. § 78n(a)(1), and proxy voting advice "implicates interests beyond those" of the investors "who utilize it when voting," 85 Fed. Reg. at 55,086. The Commission considered *all* interests—including those of the NAM's members—in adopting the Final Rules.

ISS also asserts (at 18) that the Commission never made a "'*finding*[ ]' of material errors or inaccuracies in proxy voting advice," and thus claims (at 19 n.4) that *Chenery* bars any "reliance on purported 'errors' or 'inaccuracies'" in justifying the Final Rules. ISS is wrong.

In adopting the Final Rules, the Commission expressly recognized the high "incidence of errors, mistakes, and deficiencies in voting advice that [issuers] believe exists." 85 Fed. Reg. at 55,103. While the Commission also acknowledged comments that "argued that there was insufficient evidence of inaccuracies or other problems with proxy voting advice," *id.* at 55,107, the Commission never credited them. Those comments simply stated that "most of the claimed 'errors'" were not technically "errors," but were more accurately labeled "disagreements on analysis and methodologies." AR437 at 40. The Commission explained that even if "there are no errors in the advice," 85 Fed. Reg. at 55,107, market participants still had "differing views about the [proxy voting advice businesses'] methodological approach or other differences of opinion," 84 Fed. Reg. at 66,530; *see* 85 Fed. Reg. at 55,107 (incorporating this reasoning). Those differences—whether labeled "errors" or not—would still be a problem that the Commission could reasonably address. Thus, the Commission was justified in finding that "measured changes designed to facilitate more complete and robust dialogue and information sharing among proxy voting advice businesses, their clients, and registrants would improve the proxy voting system, and ultimately lead to more informed decision-making." 85 Fed. Reg. at 55,107.

The Commission further explained that regulation was needed "[r]egardless" of the *actual* "incidence of errors in proxy voting advice." 85 Fed. Reg. at 55,107. Even the *perception* of errors that indisputably exists, *see id.* at 55,103 & n.255, can erode investor "confidence," *see id.* at 55,107, contrary to the "animating purpose of the Exchange Act," *United States v. O'Hagan*, 521 U.S. 642, 658 (1997). For this independent reason, the Commission was justified in ensuring that investors "have timely access to transparent, accurate, and complete information." 85 Fed. Reg. at 55,107.

"[C]hanging market conditions" provide yet another basis for the Commission's actions. 85 Fed. Reg. at 55,085. As the Commission explained, "institutional investors ... hold an increasingly significant portion of shares in U.S. public companies," and "proxy voting advice businesses today are uniquely situated to influence the voting decisions of [those] investors." *Id.* at 55,118. This is not "sheer speculation," ISS Reply 20, but objective information about the state of markets that the Commission is charged with regulating. The Commission could reasonably rely on its "predictive judgment," *Sorenson Commc'ns, LLC v. FCC*, 897 F.3d 214, 230 (D.C. Cir. 2018), and take "prophylactic" steps to "prevent potential problems" that could arise from the changing conditions, *Stilwell v. Office of Thrift Supervision*, 569 F.3d 514, 519 (D.C. Cir. 2009) (Kavanaugh, J.). An agency, after all, "need not suffer the flood before building the levee." *Id.*

2. Given the more-than-adequate justification for the Final Rules, ISS pivots (at 22–23) to quibbling with the Commission's cost-benefit analysis.

ISS first frets (at 22) that the Commission over-relied on a qualitative (as opposed to a quantitative) analysis. But ISS concedes "that agencies can rely upon qualitative evidence." ISS Reply 22; *see, e.g.*, *Chamber of Commerce v. SEC*, 412 F.3d 133, 142 (D.C. Cir. 2005) ("[W]e are acutely aware that an agency need not—indeed cannot—base its every action upon empirical data; depending upon the nature of the problem, an agency may be 'entitled to conduct ... a general analysis based on informed conjecture.'" (omission in original) (quoting *Melcher v. FCC*, 134 F.3d 1143, 1158 (D.C. Cir. 1998))). Here, the Commission reasonably explained that estimating certain costs and benefits "was not possible." *Bus. Roundtable v. SEC*, 647 F.3d 1144, 1150 (D.C. Cir. 2011); *see, e.g.*, 85 Fed. Reg. at 55,136 ("While some proxy voting advice businesses may already have systems in place to address some or all of these requirements, we do not have data that would allow us to estimate the costs associated with modifying or developing these systems and methods

to encompass all registrants." (footnote omitted)); *id.* at 55,137 ("Because the final amendments permit proxy voting advice businesses substantial flexibility in satisfying [a new] condition, we expect proxy voting advice businesses to implement mechanisms differently depending on, among other things, their own facts and circumstances and the nature of their client bases. Thus, the overall costs of satisfying this condition are difficult to quantify."). And ISS fails to identify any "empirical evidence" that "was readily available," *Bus. Roundtable*, 647 F.3d at 1150, or that the Commission should otherwise have considered. Accordingly, the Commission's "discussion of unquantifiable benefits fulfill[ed] its statutory obligation to consider and evaluate potential costs and benefits." *Lindeen v. SEC*, 825 F.3d 646, 658 (D.C. Cir. 2016); *see also Chamber of Commerce*, 412 F.3d at 142 ("The Commission's decision not to do an empirical study does not make that an unreasoned decision.").

The Commission's cost-benefit discussion did not, as ISS claims (at 23), "treat benefits and costs according to different standards." The Commission plainly engaged in an extensive qualitative analysis of costs and benefits *alike*. *See* 85 Fed. Reg. at 55,132–40. Nor did the Commission "use[ ] the lack of empirical data regarding costs to discount the importance of those costs," while drawing the "opposite inference from the lack of empirical data regarding benefits." ISS Reply 23. While the Commission observed that the costs were "difficult to quantify," it concluded that the benefits outweighed the costs for an entirely different reason: "To the extent proxy voting advice businesses *already have similar systems in place*, any additional direct cost [from installing those systems] may be limited." 85 Fed. Reg. at 55,137 (emphasis added). That conclusion was entirely reasonable; the Commission adequately analyzed the economic consequences of the Final Rules.

B. The Advisers Act Insufficiently Regulates Proxy Voting Advice Businesses.

ISS argues at length (at 2, 14, 19, 24–27) that proxy voting advice businesses could adequately be regulated under the Investment Advisers Act, and faults the Commission (at 25) for not definitively deciding whether such businesses fall within the Act's reach. ISS entirely ignores, however, the Commission's response that the Final Rules should apply to proxy voting advice businesses "*[r]egardless of the applicability of the Advisers Act*." 85 Fed. Reg. at 55,086 (emphasis added). The Commission reasonably explained that the Advisers Act is narrowly focused on an advisor's "fiduciary duty to clients," while proxy voting advice affects—and the proxy solicitation rules protect—broader interests, including those of other shareholders, the issuer, and the markets generally. *Id.*; *see also* NAM SJ Mem. 27–28.

ISS argues (at 28) that these broader interests could adequately be protected by regulating the quality of proxy voting advice through the Advisers Act. That is wrong. ISS concedes that, through the Advisers Act, the Commission could only "compel an advisor to [make disclosure] *to her customer*,' but could not 'expand[ ] disclosure to the issuer.'" ISS Reply 28 (alterations in original; emphasis added). Expanding disclosure to the issuer, however, is a key component of ensuring that investors receive timely access to all relevant information. *See* 85 Fed. Reg. at 55,107. If the issuer, for example, does not receive a copy of the proxy voting business's recommendation, then the issuer cannot even attempt to correct errors in, explain, or contextualize that advice, depriving all investors of the "complete and robust dialogue" that the Final Rules seek to provide. *Id.*

Another concession from ISS further confirms that the Advisers Act does not permit adequate regulation of proxy voting advice: The Advisers Act is concerned "*solely*" with the "best interests" of a proxy voting advice businesses' "clients," ISS Reply 28; it does not permit the SEC "to promote 'broader' interests," *id.*, by, for example, seeking a more thorough analysis than the

institutional investor may otherwise desire. It is only Section 14(a) of the Exchange Act that permits the SEC to prescribe regulations in the broader "public interest," which is exactly what the SEC did here. 15 U.S.C. § 78n(a)(1). When an institutional investor spends time, money, and resources analyzing an issue up for a proxy vote—and hires a proxy voting advice business to do the same—the investor directly benefits in the form of a "more informed proxy voting decision[ ]." 85 Fed. Reg. at 55,107. The Exchange Act empowers the Commission to ensure that "all" the other "shareholders of the registrant" benefit from more informed decisionmaking, *id.* at 55,086 (footnote omitted), "including [those] shareholders that [did] not use [the] proxy voting advice," *id.* at 55,107; *see also id.* at 55,086 (the advice "implicates interests beyond those of the clients who utilize it when voting"). The Exchange Act reaches a different set of concerns from those affected by the Advisers Act and permits a different regulatory approach.

ISS also misconstrues (at 29) the Commission's distinction between the "principles-based nature" of the Advisers Act's fiduciary duties and the "principles-based nature" of the Final Rules. Both are principles-based, but the key point is that the Advisers Act and the Final Rules apply *different* principles—not that the Advisers Act is inadequate *because* it is principles-based. As discussed, the Advisers Act is focused "solely" on a proxy voting advice business' relationship with its clients, ISS Reply 28, while Section 14(a) concerns broader interests. The latter is a more appropriate regulatory regime for proxy voting advice.

Regardless, ISS's argument incorrectly assumes that the Exchange Act and the Advisers Act necessarily govern "different, mutually exclusive, spheres of conduct." *Lorenzo v. SEC*, 139 S. Ct. 1094, 1102 (2019). On the contrary, there is "considerable overlap" among the securities laws, *id.*, and the Commission may reasonably choose which regulatory regime is best suited to address the particular problems it has identified.

C. ISS Mischaracterizes The Commission's Longstanding Policy.

1. Contrary to ISS's assertion (at 29–33), the Commission has long held that proxy voting advice is a form of solicitation. Indeed, ISS's recounting omits its *own* concessions to the Commission that it is properly regulated under the proxy solicitation rules.

In 1964, the Commission recognized that "[m]aterial distributed during a period while proxy solicitation is in progress, which comments upon the issues to be voted on or which suggests how the stockholder should vote, would constitute soliciting material." *Broker-Dealer Participation in Proxy Solicitations*, 29 Fed. Reg. 341, 341 (Jan. 15, 1964). In an effort to dodge the obvious import of this plain statement, ISS selectively and misleadingly quotes from the 1964 Release. According to ISS, the 1964 Release provided that "ordinary investment advisory material distributed in the ordinary course of business is not necessarily a solicitation." ISS Reply 31 (quoting 29 Fed. Reg. at 342). ISS omits the critical fact that the Commission was addressing "the ordinary distribution of research reports, market letters, etc., *which do not refer to any question to be decided by the security holders*." 29 Fed. Reg. at 342 (emphasis added). ISS, of course, *does* distribute materials that address questions to be decided by securities holders, which is what this case is all about, and for that reason, its recommendations "constitute soliciting material." *Id.* at 341.

The 1979 Release is even worse for ISS's case. There, through notice-and-comment rulemaking, the Commission exempted the "furnishing of proxy voting advice" from some of the regulatory requirements applicable to proxy solicitations—necessarily presupposing that proxy voting advice is solicitation. 44 Fed. Reg. at 68,770. ISS responds (at 32) that the 1979 Release was not addressing ISS's line of work. But ISS itself has argued that it was "exempt from the SEC's proxy filing requirements under" the exemption created by the 1979 Release. *Institutional Shareholder Services, Inc.*, 1991 WL 179448, at *4 (SEC No-Action Letter Dec. 15, 1988). And the Commission, in 1992, later agreed, ruling that "proxy advisory services" are "covered by the exemption"

created in the 1979 Release. *Regulation of Communications Among Shareholders*, 57 Fed. Reg. 48,276, 48,282 n.41 (Oct. 22, 1992).

ISS maintains (at 32) that the 1992 Release "made no attempt to ... address the threshold question of whether a fiduciary proxy adviser like ISS engages in solicitation." But in the 1992 Release, the Commission specifically ruled on the no-action request submitted by "Institutional Shareholder Services, Inc.," and held that such "proxy advisory services" would generally be exempt from some of the requirements applicable to solicitations. 57 Fed. Reg. at 48,282 n.41. That ruling again presupposes that proxy voting advice in general, and ISS's proxy voting advice in particular, are solicitations in need of an exemption.

Against this clear evidence, ISS insists (at 32) that 2019 was the "first time" the Commission recognized proxy voting advice as a form of solicitation. But that cannot be squared with the substantial body of scholarship and commentary showing that everyone, including ISS's main competitor, had already known for decades that proxy voting advice businesses were engaged in solicitation.[3] ISS does not address these materials.

ISS also overlooks its own comments made to the Commission leading up to the 1992 Release, in which ISS admitted that its "materials *remain subject* to the antifraud proscriptions of Rule 14a-9"—proscriptions that apply only to entities engaged in solicitation. Exhibit A at 4. ISS's own comments therefore belie its contention now that the Commission has imposed "new

[3] *See, e.g.*, Bernard S. Black, *Shareholder Passivity Reexamined*, 89 Mich. L. Rev. 520, 530 (1990); John C. Coffee, Jr., *Liquidity Versus Control: The Institutional Investor as Corporate Monitor*, 91 Colum. L. Rev. 1277, 1358 (1991); Sagiv Edelman, *Proxy Advisory Firms: A Guide for Regulatory Reform*, 62 Emory L.J. 1369, 1378 (2013); Douglas G. Smith, *A Comparative Analysis of the Proxy Machinery in Germany, Japan, and the United States*, 58 U. Pitt. L. Rev. 145, 201 n.284 (1996); Katherine H. Rabin, CEO, Glass, Lewis & Co., *Statement to the U.S. House of Representatives Committee on Financial Services: Markup of H.R. 5983, the "Financial CHOICE Act of 2016,"* at 3 (Sept. 13, 2016), https://www.glasslewis.com/wp-content/uploads/2016/09/2016_0912_Glass-Lewis-Statement-re-H.R.-5983_final.pdf.

liability" under "Rule 14a-9" because of the Final Rules. ISS SJ Mem. 32. In its 1991 submission, ISS forthrightly "welcome[d] the Commission's acknowledgement of the unique function of shareholder advisory services, like ISS, *as participants in the solicitation process*." Exhibit A at 1 (emphasis added). And while ISS argued that it should not be "covered by the *entire* panoply of the Proxy Rules," *id.* at 2 (emphasis added), its position presupposed that it was then, as it is now, engaged in solicitation and merely *exempted* from certain requirements.

2. ISS's cursory discussion of "reliance" interests (at 33) fails for the same reason as its attack on the SEC's supposed change in position (at 29): the Commission has long considered the furnishing of proxy voting advice to be a form of solicitation. ISS could not have reasonably relied on an agency interpretation of "solicit" that did not exist. *See Estes v. U.S. Dep't of Treasury*, 219 F. Supp. 3d 17, 33 (D.D.C. 2016). In any event, the fact that in 1988 "ISS sought assurance that it could rely on an exemption from the solicitation rules," ISS Reply 32, shows that ISS has known for decades that its activities could be considered a form of solicitation.

III. Rules 14a-2(b)(9)(ii)(A) And (B) Do Not Violate the First Amendment.

As set forth in the NAM's cross-motion and opposition, *see* NAM SJ Mem. 32–43, and that of the Commission, SEC SJ Mem. 43–45, the Final Rules do not violate the First Amendment. ISS's attempts to salvage its First Amendment challenge are meritless.

A. ISS's New First Amendment Theories Are Waived.

Contrary to ISS's mischaracterizations, the NAM has not argued that the Final Rules are "not subject to *any* First Amendment scrutiny." ISS Reply 34. There is no need for such a sweeping argument because ISS's limited First Amendment challenge is fundamentally unsound.

ISS mischaracterizes the NAM's argument to divert attention from an obvious and case-dispositive defect in its purported "compelled speech" claim: ISS fails to make any First Amendment challenge to any regulatory provision that even arguably forces it to speak. The First

Amended Complaint challenges only the requirements for the exemption from the information, filing, and disclosure requirements if "proxy advisers provide their vote recommendations to issuers and disseminate issuers' responses." FAC ¶ 94; *see also id.* ¶¶ 95–97. If there were any doubt, ISS's motion for summary judgment confirms that ISS is challenging only "two new mandates on proxy advisers"—what ISS terms the "'issuer-review' rule" and the "'issuer-response' rule." ISS SJ Mem. 37. But these beneficial *exemptions* from the separate filing and disclosure requirements of the proxy rules do not compel ISS to speak at all. ISS never alleged or argued that any other provisions of the Final Rules violate the First Amendment in any way. ISS SJ Mem. 38–44.

Belatedly recognizing its error, ISS tries to change and broaden its First Amendment challenge in its reply brief. It suggests that its *statutory* challenge to the applicability of the general information and filing proxy rules somehow implied that it was also challenging them under the First Amendment, ISS Reply 34, and that its free speech rights cannot be conditioned on receiving a benefit, *id.* at 34–35. If ISS thought these theories had merit, ISS could have pressed them in its complaint and motion for summary judgment, but it failed to do so. It is black-letter law that "'issues not raised until the reply brief are waived.'" *Bloche v. Dep't of Def.*, 414 F. Supp. 3d 6, 23 n.5 (D.D.C. 2019) (citation omitted); *Elmore v. Washington Metro. Area Transit Auth.*, No. 14-CV-00915 (APM), 2016 WL 10789354, at *2 (D.D.C. July 29, 2016) (Mehta, J.) (acknowledging that the Court will "not consider [an] issue … [when] raised it for the first time in its reply brief"); *Am. Waterways Operators v. Wheeler*, No. 18-CV-02933 (APM), 2020 WL 7024195, at *11 n.4 (D.D.C. Nov. 30, 2020) (Mehta, J.) (issue forfeited when "raised … in the[ ] reply brief" for the first time); *Atlanta Channel, Inc. v. Solomon*, No. CV 15-1823 (RC), 2020 WL 1984296, at *11 n.7 (D.D.C. Apr. 27, 2020); *Walker v. Pharm. Research & Mfrs. of Am.*, 461 F. Supp. 2d 52, 59 n.9 (D.D.C. 2006). This alone is sufficient to defeat ISS's First Amendment challenge.

Even if ISS's new First Amendment theories were not waived, they are meritless. ISS's challenge to the applicability of the proxy rules' information, filing, and disclosure requirements is a purely statutory claim that has nothing whatsoever to do with speech. As discussed in Part I, *supra*, ISS's statutory challenge fails because the SEC clearly has authority under Section 14(a) to regulate proxy voting advice businesses. And ISS's poorly developed unconstitutional conditions argument fails because, among other reasons, requiring a party that chooses to solicit a proxy to make a full and accurate disclosure for the benefit of markets is a cornerstone of the securities laws and is neither compelled speech nor an unconstitutional condition on speech. *See Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447, 456 (1978) ("[T]he exchange of information about securities" and "corporate proxy statements" are both examples "of communications that are regulated without offending the First Amendment[.]"); *Full Value Advisors, LLC v. SEC*, 633 F.3d 1101, 1108–09 (D.C. Cir. 2011) (upholding disclosures that are "indistinguishable from other underlying and oft unnoticed forms of disclosure the Government requires").

B. The Final Rules Are Viewpoint And Content Neutral.

1. ISS fails "the 'most basic ... test for viewpoint discrimination'" because it cannot demonstrate that "within the relevant subject category ... the government has singled out a subset of messages for disfavor *based on the views expressed*." *Zukerman v. U.S. Postal Serv.*, 961 F.3d 431, 446 (D.C. Cir. 2020) (first omission in original; emphasis added).

On their face, the Final Rules apply "regardless of the position a proxy voting advice business takes." SEC SJ Mem. 42. Despite the rules' plainly neutral text, ISS's claim of viewpoint discrimination boils down to the unsupported assertion that "[i]n practice," the Final Rules favor management-backed proposals. ISS Reply 37. However, ISS cites no factual record documenting this "practice," relying instead on its sweeping assertion that there is "no conceivable reason" for an issuer to prepare a written response to proxy advice unless "it *disagreed* with the adviser's

analysis or recommendation." *Id.* It takes little imagination to envision scenarios in which an issuer might wish to comment favorably or even neutrally on proxy advice, and ISS must show that the Final Rules are unconstitutional in all their applications when bringing a facial First Amendment Challenge such as this. *See Gen. Elec. Co. v. Jackson*, 610 F.3d 110, 117 (D.C. Cir. 2010) (facial challenge requires "establish[ing] either that no set of circumstances exists under which [a regulation] would be valid, or that [those provisions] lack [ ] any plainly legitimate sweep") (third and fourth alterations in original; quotation marks omitted); *Elk Run Coal Co. v. U.S. Dep't of Labor*, 804 F. Supp. 2d 8, 22 (D.D.C. 2011) (same). In any event, the Final Rules allow proxy voting advice businesses substantial discretion to develop disclosure procedures regardless of the position taken. *E.g.*, 85 Fed. Reg. at 55,101. The neutrality of the rules' text, the absence of any documented discrimination, and the substantial discretion vested in proxy voting advice businesses destroy any claim of viewpoint discrimination.

Pacific Gas & Electric Co. v. Public Utilities Commission of California, 475 U.S. 1 (1986), is not to the contrary. There, California's public utilities regulator had ordered PG&E to disseminate the editorial materials of an advocacy group critical of the utility, *id.* at 5–7, and the Supreme Court held that a blanket order compelling a private company to provide a forum for "hostile views" violated the First Amendment, *id.* at 14. Importantly, however, the Court expressly distinguished speech involving communications by a corporation to its shareholders—the situation at issue here. *See id.* at 14 n.10; *see also* SEC SJ Mem. 40. Moreover, the utilities commission expressly limited access *only* to those who "disagree[d]" with and were "hostile" to the utility's views, creating a risk that the utility might conclude that "the safe course [was] to avoid controversy" and stop speaking altogether, "thereby reducing the free flow of information and ideas that the First Amendment seeks to promote." 475 U.S. at 13–14. The Final Rules are not remotely

analogous. They apply irrespective of whether the issuer and the proxy voting advice business agree, and they promote, rather than reduce, the free flow of information. *See* SEC SJ Mem. 42; 85 Fed. Reg. at 55,107 (explaining the informational benefits of such disclosure). ISS does not contend that the Final Rules might chill its own speech. Unlike the access order in *PG&E*, the Final Rules also give ISS substantial discretion to devise any "mechanism" that reasonably allows shareholders to become aware of pertinent written statements by the issuer that are available in another forum. Rule 14a-2(b)(9)(ii)(B). *PG&E* therefore is inapposite.

2. ISS also fails to show that the Final Rules are impermissible content-based restrictions on speech. The challenged exemptions from the proxy rules' general reporting and disclosure requirements do not "compel" ISS to "speak a particular message" or "alter the content of [its] speech," ISS Reply 38 (citation omitted); ISS is free to forgo the benefits afforded by the exemptions and comply instead with the proxy rules' broader regulatory requirements. ISS does not contend that *those* requirements, from which ISS has sought exemptions in the past, are an unconstitutional burden on its speech. *See supra* Parts II.C., III.A.

Even if the challenged exemptions could be viewed as somehow compelling speech, such disclosure requirements are commonplace in the securities laws and "do not prevent [proxy voting advice businesses] from conveying any additional information." *Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 250 (2010). The Final Rules also do not draw "distinctions based on the message a speaker conveys," *Barr v. Am. Ass'n of Political Consultants, Inc.*, 140 S. Ct. 2335, 2346 (2020) (plurality op.); *id.* at 2364 (Gorsuch, J., concurring), any more than Section 14(a) of the Exchange Act draws distinctions based on who is engaging in "solicitation." The Final Rules merely *incentivize* proxy voting advice businesses to make certain beneficial disclosures as a trade-off to complying with more onerous regulatory requirements. It is not necessary

"'to examine the content of'" ISS's proxy voting advice to know whether ISS can invoke the exemptions at issue, *Pursuing Am.'s Greatness v. FEC*, 831 F.3d 500, 509 (D.C. Cir. 2016) (citation omitted), and therefore there is no content-based regulation of speech here.

C. The Final Rules Pass Any Applicable First Amendment Scrutiny.

1. At most, the Final Rules are a routine, commercial speech disclosure in the arena of securities regulation and readily pass scrutiny under *Zauderer v. Office of Disciplinary Counsel*, 471 U.S. 626 (1985). The challenged exemptions are minimalist in their approach, giving proxy voting advice businesses substantial discretion and flexibility in crafting mechanisms by which to qualify for the exemption. *See* Rules 14a-2(b)(9)(i); (b)(9)(ii)(A), (B). The challenged exemptions also advance compelling interests, including "promot[ing] the reliability and completeness of information available to investors and those acting on their behalf at the time they make voting determinations," 85 Fed. Reg. at 55,107; ensuring "the factual accuracy of proxy voting advice," *id.*; and improving of "the mix of information available to shareholders in a manner that is compatible with the complex and time-sensitive proxy voting advice infrastructure that currently exists," *id.* at 55,110. Such interests have "shaped our federal securities laws since their inception and [were] a principal factor in the Commission's adoption of these amendments." *Id.* at 55,107.

ISS argues that *Zauderer* does not apply because any disclosures made under the exemptions would not be "purely factual and uncontroversial." ISS Reply 42. However, the challenged exemptions do not require ISS to disclose any non-factual information; they merely require a "mechanism" by which clients "can reasonably be expected to become aware of any written statements regarding its proxy voting advice by registrants who are the subject of such advice." Rule 14a-2(b)(9)(ii)(B). A proxy voting advice business retains substantial "discretion … to choose the solution it deems suitable" for satisfying this exemption. 85 Fed. Reg. 55,101.

2. The Final Rules also pass scrutiny under *Central Hudson Gas & Electric Corp. v. Public Service Comm'n of New York*, 447 U.S. 557 (1980), because the Final Rules directly and materially advance a substantial government interest. NAM SJ Mem. 41–44.

Contrary to ISS's assertion (at 43), the Commission gave substantial reasons for the need for the Final Rules. *See supra* pp. 10–16. That reasoning is well supported by the record.

ISS contends (at 43–44) that that the Commission "brushed aside" various less restrictive alternatives, but the argument is difficult to credit. The Commission could have denied proxy voting advice businesses any exemptions from the proxy rules' general reporting and information requirements, but it chose instead to offer flexible exemptions and to give proxy voting advice businesses discretion in how they choose to qualify for those exemptions. Moreover, as the Commission made clear, there was a serious need to establish rules "in a manner that is compatible with the complex *and time-sensitive proxy voting advice infrastructure that currently exists*." 85 Fed. Reg. at 55,110 (emphasis added). Under the *only* alternative proposal that ISS identifies, there would be *no* means for an issuer to address matters in proxy advice about the issuer before voting occurs. *See id.* at 55,144 (discussing timing issues created by robo-voting); ISS SJ Mem. 43. Because ISS points to no less restrictive alternative that would solve the problems the Commission identified, its tailoring argument fails. *See, e.g.*, *Harrell v. Fla. Bar*, 608 F.3d 1241, 1271 (11th Cir. 2010) (First Amendment claim failed where challenger "neither suggested a less restrictive means of effectuating the [government's] important goals, nor explained how the" challenged regulation "imposes a burden that is unreasonable in relation to the goal"); *Wright v. Chief of Transit Police*, 558 F.2d 67, 74 (2d Cir. 1977) ("The plaintiffs have an obligation to at least suggest one less restrictive alternative to the trial court.").

CONCLUSION

ISS's motion for summary judgment should be denied, and the NAM's motion granted.

Dated: December 9, 2020

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on this 9th day of December, 2020, I caused a copy of the foregoing document to be served on all parties through the Court's CM/ECF system.

/s/ Helgi C. Walker
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