

SEC Charges Investment Adviser for Proxy Voting Rule Violations

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In the first enforcement action of its kind, the Securities and Exchange Commission has charged a registered investment adviser for willfully violating a SEC proxy voting rule and the investment adviser and its former chief operating officer were censured and fined \$300,000 and \$50,000, respectively. *In the Matter of INTECH Investment Management LLC*, Investment Advisers Act Rel. No. 2872 (May 7, 2009). The manner in which registered investment companies vote their shares on behalf of clients is important because they are reportedly the largest group of investors in U.S. public companies, currently holding over a quarter of U.S. public companies' stock.

The SEC proxy voting rule, Investment Advisers Act Rule 206(4)-6 adopted in 2003, requires a registered investment adviser that exercises voting authority over client proxies to adopt and disclose policies and procedures reasonably designed to ensure that the adviser votes in the best interests of clients. The investment adviser's policies and procedures must describe how the adviser addresses material conflicts between the adviser's interests and those of its clients with respect to proxy voting.

In 2002, in deciding how to vote its clients' securities, the investment management company chose to rely on a platform offered by Institutional Shareholder Services (ISS, now known as Riskmetrics). After adopting this platform, the investment management company received complaints from some of its union-affiliated clients, and also scored in the middle tier of an annual AFL-CIO survey ranking investment advisers that measured how closely the investment management company's voting record matched AFL-CIO recommendations. In 2003, the investment management company switched to an ISS policy that followed AFL-CIO recommendations and, as a result, its annual AFL-CIO survey score increased to 100%, but the switch also resulted in some of its clients inquiring as to why more of the investment management company's votes were against management, as compared to 2002.

The SEC found that the policies and procedures that the investment management company released in 2003 after switching to the AFL-CIO-based voting plan violated the proxy voting rule. Specifically, the investment management company did not disclose that the ISS policy to which it had switched in 2003 followed AFL-CIO voting recommendations. Moreover, the investment management company did not address in its policy the possible conflict between clients not affiliated with unions and a policy of voting uniformly with the AFL-CIO nor did it disclose that alignment of its voting policy with the AFL-CIO would improve its score on the AFL-CIO survey and could facilitate the investment management company's retention and recruitment of union-affiliated clients. As a result, the SEC found that the investment management company willfully violated the proxy voting rule, and that its former chief operating officer aided and abetted those violations.

The SEC's action suggests an increased focus on enforcing the investment adviser's proxy voting rule which should lead to greater transparency for voting policies and procedures of registered investment advisers and better disclosure of material conflicts that may exist between those policies and the interests of certain of the investment adviser's clients.

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