

NIRI's 2022 Leadership and Legislative Fly-In

By, Kimberly Esterkin

The Investor Relations Officer (IRO) has many hats one of which I learned more intently about last week – the advocacy hat. It seems natural that an IRO would serve in an advocacy role. We advocate for our companies and management teams on a daily basis. However, what is not necessarily natural for an IRO is advocating on behalf of regulatory issues – issues which are at the forefront of increasing transparency, speeding up information transmission or modernizing rulings that were developed decades before but never updated and continue to impact public issuers day in and day out.

As President of the National Investor Relations Institute (NIRI) of Los Angeles, I was offered the unique opportunity to join fellow IROs at a Legislative and Leadership Fly-in on September 21st and 22nd in Washington, DC. Over the two-day period, we held an interactive Zoom session with the Securities Exchange Commission (note they are still working remotely at this time), and then made our way to Capitol Hill where we met with Congressmen and women representing our respective legislative districts. At each of these meetings, we asked either for voting support or co-sponsorship of a bill already submitted.

As lobbying is certainly not our day-to-day job, prior to making our way to Congress, NIRI professionals were provided a crash course on lobbying hosted by Niels Holch, Founding Partner of Holch & Erickson, LLP, and David Dragics, Independent Consultant and former head of IR for CACI International. Niels and David educated us on lobbying best practices, which included lessons such as: 1) the effective use of staff member time; 2) the understanding that we should never assume House staff members, unless a member of a financial committee, have a deep knowledge of public companies and securities law; and 3) that you should never leave your first meeting without learning directions for how to get to your next one. In some ways, it sounds just like talking to a new investor!

It was quite inspiring to have the opportunity to present our case to senior legislative staffers, while simultaneously elevating the role of investor relations and representing our individual companies and management teams. I personally was in a group of individuals from Texas, California and Denver, and together we spoke to the offices of Lizzie Fletcher (D-TX), Mike Thompson (D-CA) and Diana DeGette (D-CO). NIRI represents professionals across the United States accounting for over 1,600 publicly traded companies, so as my group spoke to the South and Western regions of the U.S., we also had groups speak to representatives from other geographic regions.

Key Legislative Issues Discussed with Congress by NIRI Professionals:

1. 13F Modernization:
    a. Current SEC rules require investment managers with at least $100 million in assets disclose their ownership positions within 45 days of the end of a calendar quarter. This is done through a 13F filing which stands for section 13(f) of the Securities Exchange Act.
    b. These rules were first developed in 1975 and despite major changes in the speed and methods by which we trade securities today, have not been updated since. In their current form, they are therefore outdated and have become a barrier to receiving timely information on public company investors.
    c. To put this into perspective. There are only 4 days per 250 trading days a year where an issuer knows which institutions hold their stock. In other words, only 1.6% of the year does a public company know who held their stock at the end of a quarter.
    d. Further, there's ways for investors to push that time frame ever longer. A hedge fund, for example, can acquire a 4.9% equity stake in a public company on January 2nd but due to 13F rules not have to disclose that position to the marketplace until May 15th, more than 4 months later.
    e. H.R. 4618 – the Short Sale Transparency and Market Fairness Act – has been approved by the House Financial Services Committee. The bill was authored by Committee Chairwoman Maxine Waters and is supported by NIRI. The bill asks to move the reporting process for 13F filers to a more reasonable time frame, i.e. from quarterly to monthly reporting.
    f. **Our ask**: NIRI asked for Congress to vote YES on H.R. 4618 should it be brought again to the House floor. It was previously voted against as it was packaged with two other pieces of legislation that were not supported.

2. Disclosure of Short Sale Positions:
    a. Similar to wanting more transparency around institutional holdings, NIRI is arguing for improved information on short sale positions.
    b. By way of background, a short sale occurs when an investor borrows shares of stock from another investor with a promise to return an equal amount of shares at some time in the future. A profit is made if the shares decline in price and the investor is able to return the shares borrowed at a lower price.
    c. The SEC does not require investors to publicly disclose large short positions. Instead, we are able to access an aggregated report of short positions (i.e. not by individual shareholder) twice per month. IROs and issuers, however, are looking for manager-level information on short positions.
    d. While NIRI recognizes that information on the manager holding shorts in a company could result in an attack on short sellers, the benefits of knowing who may be shorting a company's stock and thus ultimately impeding its potential for growth far outweigh the chance of retaliation on the short seller.
    e. This spring, the SEC proposed a new regulation which would require 13(f) managers holding large short positions to file a Form SHO with the SEC within 14 calendar days after the end of each month. This short position would be kept confidential by the SEC to

protect the identities of the reporting investment manager and to avoid public disclosure of their short positions which could hinder their investment strategies.

f. Once filed, the SEC will publicly disclose these positions on an aggregated basis which is information issuers already receive.
g. **Our ask:** NIRI would like to take that ruling one step further in which the SEC would consider providing the manager information not the aggregated information on Form SHO with each public company on a confidential basis. In order to ensure confidentiality, the SEC would need to include a provision in its Final Rule that requires the identity of any information shared to be protected by the company in the same way it would protect material nonpublic information.

3. Proxy Advisory Firm Regulation:
    a. Institutional Shareholder Services (ISS) and Glass Lewis (GL) operate an oligopoly when it comes to proxy voting advice. More than 90% of institutional investors use one of these two firms to vote their proxies.
    b. Unfortunately, there is a lack of transparency in the way these two advisors operate. Moreover, their consulting arms may present conflicts of interest. For example, should ISS provide a negative recommendation, their consultants for a fee will help that same company address the issues raised in their proxy report.
    c. Additionally, there are often questions about the validity of the information in these reports, such as inappropriate methodologies for metrics used in calculations around short and long-term executive compensation.
    d. Large money managers such as BlackRock and Vanguard have their own proxy departments and while they do receive ISS and GL reports, they have the resources to vote their own views during the proxy process. Smaller and mid-sized investment managers do not have the ability to vote all of their positions, and so by default they vote in line with these advisory firms. ISS and GL influence as much as 20% of the vote in an annual shareholder meeting.
    e. Public companies have been advocating for more oversight of these firms for over a decade. With robovoting all the more common these days, if a report goes out with a mistake and an institution immediately votes using that report's recommendations, even if an issuer gets the mistake fixed, reaching out to institutions who already voted their proxy is quite arduous.
    f. Interestingly enough, for years, ISS enabled companies listed in the S&P 500 to see their reports before they were published, providing management of these very large market cap companies the unique ability to review, point out mistakes, and revise their reports before voting took place. It worked well for some time, though companies did on occasion want extra days to review their reports.
    g. In 2020, the SEC moved forward with a regulatory proposal to oversee these advisors and a Final Rule was issued. This rule was overturned in 2021, again eliminating the ability of companies to proactively correct factual errors in proxy advisors' reports.
    h. In the lead up to the 2020 Final Rule issuers made two requests. First, was that all companies whether in the S&P 500 or not be given an advance review of their proxy reports from ISS. If that was too broad, they asked for at least those in the S&P 1500

receive a pre-look. The second request was that this review process be extended not just to ISS' reports but that of other proxy advisory firms as well.

i. While a new SEC Final Rule was issued this summer to monitor proxy firms, it ignores the ability for issuers to review their reports ahead of time.
j. **Our ask**: NIRI is asking for the SEC to reconsider its position, so that public companies can review their reports and correct factual errors before their shareholder meetings take place ultimately ensuring a more fair voting process.

Concluding Thoughts:

In addition to the aforementioned issues, during our Zoom session with the SEC on day one of the event, we spoke about several other proposals including that of 13D modernization, improvements to proxy plumbing (i.e. the NOBO system) and increased transparency of security based swaps.

The discussion is far from over, and NIRI asked for our feedback on ways to continue IROs' efforts in the advocacy process. One recommendation which I personally made was that NIRI provide opportunities for IROs and their respective companies to participate in calls with Congress and the SEC on a more regular basis. That would enable all of us to not only stay abreast of current regulatory issues but also help to push the important ones forward. NIRI is currently considering this opportunity.

It's pretty amazing to see the legal sausage making in the works. In my own humble opinion, at the 2022 Legislative and Leadership Fly-in NIRI members put forth a valiant grassroots effort to share their viewpoints and potentially open some more eyes and ears to the need for equity market reform. Every effort and voice counts, just like every shareholder vote can make a difference.

Disclaimer: These prior pages are notes taken during the NIRI Legislative and Leadership Fly-in event and are not meant to be a voting or legislative guide. The above notes do not necessarily reflect the viewpoints of NIRI Los Angeles or of Addo Investor Relations. Please refer to additional disclosures and comment letters written by NIRI and issuers to the SEC referring to these topics for additional inputs and information.