

arguments why an adviser that accepts voting authority ought not be required to have procedures in place to ensure that it meets its fiduciary obligations to clients.⁹

Advisers that have implicit as well as explicit voting authority must comply with rule 206(4)–6. The rule thus applies when the advisory contract is silent but the adviser's voting authority is implied by an overall delegation of discretionary authority.¹⁰ The rule does not apply, however, to advisers that provide clients with advice about voting proxies but do not have authority to vote the proxies.¹¹

2. Policies and Procedures

Under rule 206(4)–6, advisers that exercise voting authority with respect to client securities must adopt proxy voting policies and procedures.¹² The policies and procedures must be in writing. They must be reasonably designed to ensure that the adviser votes in the best interest of clients.¹³ And they must describe how the adviser addresses material conflicts between its interests and those of its clients with respect to proxy voting.¹⁴ Most commenters supported these requirements, and many advisers

informed us that they already had written policies in place.

We did not propose, and are not adopting, specific policies or procedures for advisers. Nor are we, as some commenters requested, providing a list of approved procedures. Investment advisers registered with us are so varied that a “one-size-fits-all” approach is unworkable. By not mandating specific policies and procedures, we leave advisers the flexibility to craft policies and procedures suitable to their businesses and the nature of the conflicts they face. As noted by some commenters, some advisers (including many smaller firms) are unlikely to face any material conflicts of interest, in which case their procedures could be very simple.¹⁵

An adviser's proxy voting policies and procedures should be designed to enable the firm to resolve material conflicts of interest with its clients before voting their proxies. As we discussed above, these obligations involve both a duty to vote client proxies and a duty to vote them in the best interest of clients.¹⁶

a. Voting Client Proxies

The duty of care requires an adviser with voting authority to monitor corporate actions and vote client proxies. Therefore, the adviser should have procedures in place designed to ensure that it fulfills these duties.¹⁷ We do not suggest that an adviser that fails to vote every proxy would necessarily violate its fiduciary obligations. There may even be times when refraining from voting a proxy is in the client's best interest, such as when the adviser determines that the cost of voting the proxy exceeds the expected benefit to

the client.¹⁸ An adviser may not, however, ignore or be negligent in fulfilling the obligation it has assumed to vote client proxies.¹⁹

b. Resolving Conflicts of Interest

An adviser's policies and procedures under the rule must also address how the adviser resolves material conflicts of interest with its clients. Some commenters urged us to approve methods that would resolve material conflicts. Clearly, an adviser's policy of disclosing the conflict to clients and obtaining their consents before voting satisfies the requirements of the rule and, when implemented, fulfills the adviser's fiduciary obligations under the Advisers Act.²⁰ In the absence of client disclosure and consent,²¹ we believe that an adviser that has a material conflict of interest with its clients must take other steps designed to ensure, and must be able to demonstrate that those steps resulted in, a decision to vote the proxies that was based on the clients' best interest and was not the product of the conflict.²²

¹⁸ For example, casting a vote on a foreign security may involve additional costs such as hiring a translator or traveling to the foreign country to vote the security in person.

¹⁹ The scope of an adviser's responsibilities with respect to voting proxies would ordinarily be determined by the adviser's contracts with its clients, the disclosures it has made to its clients, and the investment policies and objectives of its clients. An adviser's fiduciary duties to a client do not necessarily require the adviser to become a “shareholder activist” by, for example, actively engaging in soliciting proxies or supporting or opposing matters before shareholders. As a practical matter, advisers will determine whether to engage in such activism based on its costs and expected benefits to clients. *Cf.* Department of Labor, Interpretive Bulletin Relating to Written Statements of Investment Policy, Including Proxy Voting Guidelines, 29 CFR 2509.94–2 at § 3 (2001).

²⁰ In this regard, we believe that an adviser to an investment company would satisfy its fiduciary obligations under the Advisers Act if, before voting the proxies, it fully discloses its conflict to the investment company's board of directors or a committee of the board and obtains the board's or committee's consent or direction to vote the proxies.

²¹ An adviser seeking a client's consent must provide the client with sufficient information regarding the matter before shareholders and the nature of the adviser's conflict to enable the client to make an informed decision to consent to the adviser's vote. Boilerplate disclosure in a client brochure regarding generalized conflicts would be inadequate.

²² Courts have taken a similar approach with respect to the business judgment rule afforded directors of corporations. When corporate directors take action notwithstanding their conflict of interest, they lose the deference that they normally receive under the “business judgment rule,” and must demonstrate that their corporate action was fair to the corporation and its shareholders. *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993). “The rationale for employing the intrinsic fairness standard is that where corporate fiduciaries, because of a conflict, are disabled from

⁹ We note that, while we are not creating an exception for smaller firms, as some commenters suggested, smaller firms without financial industry affiliates are likely to have few or even no potential conflicts of interest relating to proxy voting, in which case their procedures could be much simpler and compliance with the rule would be commensurately less burdensome.

¹⁰ Several commenters argued that the rule should not apply to advisers that have not received explicit authority to vote proxies. Advisers who believe that the application of the rule to them would be inappropriate could revise their advisory contracts (or make other disclosure to clients) to make explicit their responsibility (or lack of responsibility) for voting proxies.

¹¹ The Advisers Act's general anti-fraud provisions would, however, continue to require such advisers to disclose any material conflict to the clients receiving the advice.

¹² Rule 206(4)–6(a).

¹³ Nothing in the rule prevents an adviser from having different policies and procedures for different clients. Thus, the board of directors of an investment company could adopt and require an investment adviser to use different policies and procedures than the adviser uses with respect to its other clients.

¹⁴ Advisers' proxy voting policies and procedures should address (although the rule does not require) how the adviser will vote proxies (or what factors it will take into consideration) when voting on particular types of matters, such as changes in corporate governance structures, adoption or amendments to compensation plans (including stock options) and matters involving social issues or corporate responsibility. The policies and procedures of an adviser whose advisory activities are limited to investments in investment companies would, of course, address different matters, including, for example, approval of advisory contracts, distribution plans (“12b–1 plans”), and mergers.

¹⁵ Even the smallest firm, however, may from time to time have conflicts of interests with clients. For example, an adviser that is solicited to vote client proxies approving an increase in fees deducted from mutual fund assets pursuant to a 12b–1 plan has a conflict of interest with its clients invested in the fund if the fees are a source of compensation for the adviser.

¹⁶ While the rule allows for flexibility, it does not allow for mere boilerplate. Procedures that merely declare that all proxies will be voted in the best interests of clients would not be sufficient to meet the rule's requirements.

¹⁷ We suggested in the Proposing Release that effective procedures should identify personnel responsible for monitoring corporate actions, those responsible for making voting decisions, and those responsible for ensuring that proxies are submitted timely. Commenters felt that less detail could suffice and asked whether it was necessary for procedures to name individuals. Under the rule, advisers can write procedures that fit their firm. In a firm with few employees, those roles may be self-evident. Large firms, however, may need to clarify which department or group of employees has what responsibility in order to guard against non-compliance.