

Advisers today use various means of ensuring that proxy votes are voted in their clients' best interest and not affected by the advisers' conflicts of interest.²³ An adviser that votes securities based on a pre-determined voting policy could demonstrate that its vote was not a product of a conflict of interest if the application of the policy to the matter presented to shareholders involved little discretion on the part of the adviser.²⁴ Similarly, an adviser could demonstrate that the vote was not a product of a conflict of interest if it voted client securities, in accordance with a pre-determined policy, based upon the recommendations of an independent third party. An adviser could also suggest that the client engage another party to determine how the proxies should be voted, which would relieve the adviser of the responsibility to vote the proxies.²⁵ Other policies and procedures are also available; their effectiveness (and the effectiveness of any policies and procedures) will turn on how well they insulate the decision on how to vote client proxies from the conflict.

3. Disclose How To Obtain Voting Information

Rule 206(4)–6 requires advisers to disclose to clients how they can obtain information from the adviser on how their securities were voted.²⁶ Commenters supported advisers' disclosure of actual votes.²⁷ Many

safeguarding the interests of the stockholders to whom they owe a duty, the Court will furnish compensatory procedural safeguards by imposing upon the fiduciaries an exacting burden of establishing the utmost propriety and fairness of their actions." *Van de Walle v. Unimation, Inc.* 1991 Del. Ch. LEXIS 27, at 30 (Mar. 6, 1991).

²³ We believe an adviser that has assumed the responsibility of voting client proxies cannot fulfill its fiduciary responsibilities to its clients by merely refraining from voting the proxies. Such proxies would not be voted in the best interest of the clients.

²⁴ Of course, the pre-determined policy must be designed to further the interests of clients rather than the adviser. Thus, an adviser could not, consistent with its duty, adopt a pre-determined policy of voting proxies in favor of the management of companies with which it does business. We recognize, however, that in many cases, voting policies are not sufficiently specific to determine how the vote will be cast.

²⁵ See, e.g., Evergreen Investment Management Company, LLC, SEC Staff No-Action Letter at n. 6 (Feb. 13, 2002) (client mutual fund hired third party to vote proxies in merger contest involving the adviser's parent corporation).

²⁶ Rule 206(4)–6(b). We expect most advisers will make this disclosure in their written brochure required under rule 204–3 [17 CFR 275.204–3].

²⁷ The rule does not prescribe a client's right to this information because we do not believe a prescription is necessary. Although a few commenters suggested that the rule should prescribe a right, other commenters including investment advisers agreed with us that a client

advisers indicated that their clients, particularly institutional clients, do request this information and that the advisers already have procedures in place to facilitate clients' access to this information.

Many investors urged that rule 206(4)–6 require that advisers publicly disclose how they vote their client proxies. In a companion release, we are today adopting rules requiring that investment companies publicly disclose how they vote their proxies.²⁸ We are requiring public disclosure as a means of informing *fund shareholders* how the fund (or its adviser) voted proxies of the shareholders' fund. Public disclosure is unnecessary for advisers to communicate to each client how the adviser has voted that client's proxies. Moreover, public disclosure of proxy votes by some advisers would reveal client holdings and thus client confidences. We have determined, therefore, not to require advisers to disclose their votes publicly.

4. Describe Policies and Procedures

Rule 206(4)–6 also requires advisers to describe their proxy voting policies and procedures to clients, and upon request, to provide clients with a copy of those policies and procedures.²⁹ Commenters strongly supported this requirement, which we are adopting as proposed. The description should be a concise summary of the adviser's proxy voting process rather than a reiteration of the adviser's policies and procedures, and should indicate that a copy of the policies and procedures is available upon request. If a client requests a copy of the policies and procedures, the adviser must supply it.

B. Rule 204–2, Recordkeeping

Investment advisers expressed significant concerns with the compliance burdens of the proposed recordkeeping requirements and suggested several improvements. We are adopting the amendments to rule 204–2 with modifications that should substantially reduce those compliance burdens. Under rule 204–2, as amended, advisers must retain (i) their proxy voting policies and procedures; (ii) proxy statements received regarding client securities; (iii) records of votes they cast on behalf of clients; (iv) records of client requests for proxy

already has the right to information about how that client's securities were voted. See Restatement (Second) of Agency § 381.

²⁸ *Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies*, Investment Company Act Release No. 25922 (Jan. 31, 2003).

²⁹ Rule 206(4)–6(c).

voting information,³⁰ and (v) any documents prepared by the adviser that were material to making a decision how to vote, or that memorialized the basis for the decision.³¹ In response to suggestions from commenters, the amendments permit an adviser to rely on proxy statements filed on our EDGAR system instead of keeping its own copies, and to rely on proxy statements and records of proxy votes cast by the adviser that are maintained with a third party such as a proxy voting service, provided that the adviser has obtained an undertaking from the third party to provide a copy of the documents promptly upon request.

III. Effective Date

New rule 206(4)–6 and the amendments to rule 204–2 are effective on March 10, 2003. Advisers must comply with the new rule and amendments by August 6, 2003. By this date, advisers subject to the new rule must have adopted and implemented the required proxy voting policies and procedures. Also by this date, advisers must have provided clients with a description of their policies and procedures, and disclosure of how the clients may obtain information from the adviser on how it voted with respect to their securities.

Advisers may choose any means to make this disclosure, provided that it is clear, not "buried" in a longer document, and received by clients by August 6, 2003. For example, an adviser could send clients the disclosure together with a periodic account statement, deliver it in a separate mailing, or include it in its brochure (or Part II of Form ADV). Advisers that use their brochure or Part II to make the disclosure must deliver (not merely offer) the revised brochure to existing clients by August 6, 2003, and should accompany the delivery with a letter identifying the new disclosure.

IV. Cost-Benefit Analysis

A. Background

The Commission is sensitive to the costs and benefits resulting from its rules. While investment advisers typically exercise proxy voting authority

³⁰ As adopted, the amendments only require an adviser to keep all *written* requests from clients and any *written* response from the adviser (to either a written or an oral request).

³¹ Rule 204–2(c)(2). These records (other than proxy statements on file with our EDGAR system or maintained by a third party and proxy votes maintained by a third party) must be maintained in an easily accessible place for five years, the first two in an appropriate office of the investment adviser. Rule 204–2(e)(1). These are the same retention requirements that apply to most other books and records under rule 204–2.