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Sixth Circuit Upholds SEC's Proxy Advisor Rule Repeal, Creating Split with Fifth Circuit

On September 10, 2024, in *Chamber of Commerce of United States* v. *Securities and Exchange Commission* (the "SEC" or the "Commission"),[1] the U.S. Court of Appeals for the Sixth Circuit upheld the SEC's partial rescission (the "Rescission") of enhanced conflict-of-interest disclosure requirements for Proxy Voting Advice Businesses ("PVABs"). In doing so, the Sixth Circuit broke from the U.S. Court of Appeals for the Fifth Circuit, which, earlier this year in *National Association of Manufacturers* v. *SEC*,[2] held that the Rescission was arbitrary and capricious under the Administrative Procedure Act (the "APA"), lacking adequate justification. In *Chamber of Commerce*, however, the Sixth Circuit upheld the Rescission as neither (i) substantively deficient, because the Rescission was not arbitrary or capricious under the APA and because the SEC sufficiently analyzed the Rescission's economic consequences under the Securities Exchange Act of 1934 (the "Exchange Act"), nor (ii) procedurally deficient, because the SEC did not violate the APA's procedural requirements despite providing only 31 days for the public to comment on the Rescission. The decision creates a circuit conflict that may ultimately need to be resolved by the United States Supreme Court.

I. Factual and Procedural Background

Individual and institutional shareholders of publicly-traded companies have the right to vote on a variety of corporate governance issues relating to the companies in which they invest. The exercise of this right has raised both logistical and substantive challenges for shareholders, since shareholder voting often requires expending considerable resources to learn about the relevant issues and attend shareholder meetings.[3] For some institutional investors, this can mean casting votes at potentially thousands of shareholder meetings each year.[4]

To minimize these burdens, PVABs provide research, analysis, and voting recommendations for investors.[5] They also often serve as the investor's proxy by casting the vote directly on the investor's behalf. Despite their utility, some claim that PVABs present certain challenges for the proxy voting system because their relationships with public companies and investors can present conflicts of interest and their recommendations sometimes contain inaccurate information.[6]

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[1] 2024 WL 4132206 (6th Cir. Sept. 10, 2024).

[2] 105 F.4th 802 (5th Cir. 2024).

[3] *See Chamber of Com. of U.S.*, 2024 WL 4132206, at *1–2.

[4] *Id.* at *1 (citing Amendments to Exemptions From the Proxy Rules for Proxy Voting Advice, 84 Fed. Reg. 66518, 66519 (Dec. 4, 2019)).

[5] *Id.* at *2.

[6] *Id.*

These challenges fall within the SEC's purview because proxy voting advice is considered a form of "proxy solicitation" under the Exchange Act.[7] While the SEC has informally recognized that PVAB advice constitutes a "solicitation" under the Exchange Act—meaning that the advice is governed by the prohibition in 17 C.F.R. § 240.14a-9 on false or misleading statements in proxy materials—PVABs have historically avoided Regulation 14A's substantive and procedural requirements by qualifying for an exemption under Rule 14a-2(b)(1) or (b)(3).[8]

During the 2010s, the SEC undertook a "comprehensive review of the proxy voting infrastructure."[9] Specifically, (i) in 2010, the SEC issued a concept release seeking public comment about "the role and legal status of proxy advisory firms within the U.S. proxy system"; (ii) in 2013 and 2018, the Commission hosted roundtables to discuss the role of PVABs; and (iii) in 2014, the Commission issued a legal bulletin clarifying how PVABs may qualify for exemptions under Rule 14a-2(b).[10] These efforts culminated in the SEC releasing, in December 2019, a Notice of Proposed Rulemaking amending the application of proxy rules to PVABs.[11] The proposed rule would, according to the SEC, "enhance the accuracy, transparency of process, and material completeness of the information provided to clients" of PVABs, and would "enhance disclosures of conflicts of interest that may materially affect [PVAB] voting advice."[12]

The SEC adopted an amended version of the proposed rule in September 2020 (the "2020 Rule"). The 2020 Rule (i) codified the view that PVAB advice constituted a "solicitation" under Section 14(a) of the Exchange Act; (ii) required PVABs to disclose certain conflicts of interest in their voting advice and take certain steps to notify companies of their advice before dissemination (the "Notice-and-Awareness Conditions"); and (iii) provided, in an explanatory note to the rule, examples of material misstatements prohibited under Rule 14a-9.[13] Recognizing that the new rule would burden PVABs the most during the first year of implementation, the SEC proposed delaying enforcement until December 1, 2021.[14]

In June 2021, following Gary Gensler's appointment as SEC Chair, Chair Gensler issued a statement requiring the SEC to revisit the 2020 Rule.[15] Five months later, the SEC issued a proposed Rescission to amend the 2020 Rule by removing the Notice-and-Awareness Conditions and the explanatory note to Rule 14a-9.[16] The SEC

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[7] *Id.* Section 14(a) of the Exchange Act authorizes the SEC to regulate proxy solicitations and states that it is "unlawful for any person . . . in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors to solicit any proxy . . . in respect of any [registered] security." 15 U.S.C. § 78n(a)(1).

[8] *Id.*

[9] *Id.* (quoting Mary L. Schapiro, *Speech by SEC Chairman: Opening Statement at the SEC Open Meeting* (July 14, 2010), https://www.sec.gov/news/speech/2010/spch071410mls.htm).

[10] *Id.* (citing Commission Interpretation and Guidance Regarding the Applicability of the Proxy Rules to Proxy Voting Advice, 84 Fed. Reg. 47416, 47416 (Sept. 10, 2019)).

[11] *Id.* at *3.

[12] *Id.* (quoting 84 Fed. Reg. at 66,520). Notice of the proposed rulemaking was published to the Federal Register on December 4, 2019, and the SEC provided 60 days for public comment.

[13] *Id*.

[14] *Id*. (citing 84 Fed. Reg. at 66,554).

[15] *Id.* at *4 (citing SEC Division of Corporation Finance, *Statement on Compliance with the Commission's 2019 Interpretation and Guidance Regarding the Applicability of the Proxy Rules to Proxy Voting Advice and Amended Rules 14a-1(1), 14a-2(b), 14a-9* (June 1, 2021), https://www.sec.gov/news/public-statement/corp-fin-proxy-rules-2021-06-01).

[16] *Id*.

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provided a 31-day comment period for the proposed Rescission, and the proposed Rescission was ultimately adopted by the SEC on July 13, 2022 by a 3-2 vote.[17]

In July 2022, the United States Chamber of Commerce, Business Roundtable, and the Tennessee Chamber of Commerce and Industry (together, "Plaintiffs") sued the SEC and its Chair in the U.S. District Court for the Middle District of Tennessee, challenging the Rescission.[18] Plaintiffs argued that the Rescission was both substantively and procedurally deficient.[19] As to substantive deficiency, Plaintiffs asserted that (i) the Rescission was arbitrary and capricious under the APA and (ii) the SEC did not sufficiently analyze the Rescission's economic consequences, in violation of the Exchange Act.[20] Plaintiffs also asserted that the 31-day comment period provided by the SEC was procedurally deficient under the APA.[21]

The parties ultimately filed cross-motions for summary judgment, and on April 24, 2023, the district court denied Plaintiffs' summary judgment motion and granted the SEC's.[22] First, the district court found that the Rescission was not substantively deficient because (i) the Rescission was not arbitrary and capricious under the APA (since, among other reasons, the APA did not require the SEC to provide an analysis for the Rescission as lengthy as the analysis the SEC provided originally for the 2020 Rule) and (ii) the SEC sufficiently compared the benefits of the Notice-and-Awareness Conditions to its compliance burdens.[23] Second, the district court found that the 31-day comment period, even if "somewhat troubling," was nonetheless "within the bounds of what was legally permissible."[24] Plaintiffs appealed to the Sixth Circuit.

II. Sixth Circuit's Decision

On September 10, 2024, by a 2-1 ruling, the Sixth Circuit affirmed.[25] Reviewing the district court's decision *de novo*, the Sixth Circuit agreed that (i) the Rescission was not arbitrary or capricious under the APA, (ii) the SEC adequately analyzed the Rescission's economic consequences in accordance with the Exchange Act, and (iii) the steps taken to rescind the rule, including the shortened comment period, were not procedurally deficient under the APA.

First, the Sixth Circuit found that the Rescission was not arbitrary or capricious under the APA. It explained that the Rescission satisfied the requirements set forth by the Supreme Court in *Federal Communications Commission* v. *Fox Television Stations, Inc.*, 556 U.S. 502 (2009), under which the reasons for a new policy need not be "*better* than the reasons for the old one," but there must be "good reasons for it," and the agency must "*believe[]* it to be better, which the conscious change of course [must] adequately indicate[]."[26] Here, the court found those requirements were satisfied because the SEC both "candidly recognized" that the Rescission constituted a change in

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[17] *Id.*

[18] *Id.* at *5.

[19] *Id.*

[20] *Id.*

[21] *Id.*

[22] *See Chamber of Com. of U.S.* v. *SEC*, 670 F. Supp. 3d 537 (M.D. Tenn. 2023), *aff'd*, 2024 WL 4132206.

[23] *Id.* at 554–55, 559–61.

[24] *Id.* at 552–53.

[25] *Chamber of Com. of U.S.*, 2024 WL 4132206.

[26] *Id.* at *6 (quoting *Fox Television Stations, Inc.*, 556 U.S. at 515) (emphasis in original).

approach and acknowledged that, despite previously finding that the benefits of the 2020 Rule outweighed its costs, the SEC now "weigh[ed] those competing concerns differently."[27] In other words, because the Rescission did not rely on factual findings that were "contrary" to the findings in the 2020 Rule, the SEC did not need to provide a "more detailed explanation" for the Rescission, as would have been required under *Fox* if the SEC's action had "disregard[ed]" the "facts and circumstances" supporting the prior regulation.[28] The court also explained that the SEC did not act arbitrarily merely because the Rescission followed a change in presidential administration.[29]

Second, the court determined that the SEC adequately analyzed the Rescission's economic impact as mandated by the Exchange Act. The Exchange Act requires the SEC to "consider, in addition to the protection of investors," whether its regulatory action will "promote efficiency, competition, and capital formation" by "determin[ing] as best it can the economic implications of the rule it has proposed."[30] The Sixth Circuit found that the SEC met its burden here because the SEC adequately estimated the Rescission's impact both on PVABs and their clients—namely, the Rescission would reduce direct costs for PVABs by allowing voluntary practices to continue, and would also benefit clients inasmuch as the Rescission would reverse the increased compliance costs for PVABs that would have been passed on to clients.[31] The court also rejected Plaintiffs' argument that the SEC should not have been entitled to rely on data collected in anticipation of the 2020 Rule, explaining that the Exchange Act did not require the SEC to "forget that its earlier analysis ever happened."[32]

Third, the Sixth Circuit found that the Rescission's 31-day comment period was not procedurally deficient. The court explained that Plaintiffs' arguments were "largely formalistic," and that finding the shortened comment period procedurally deficient "would require holding the Commission to an erroneously heightened procedural standard."[33] The court also noted that Plaintiffs failed to explain *how* an "extended comment period would have enhanced the substantive record," rendering Plaintiffs' arguments an "empty gesture."[34]

Finally, in a dissent that largely mirrored the Fifth Circuit's decision in *National Association of Manufacturers*, Judge John K. Bush explained that the Rescission was both procedurally and substantively invalid and should be vacated. First, Judge Bush found that the 31-day comment period for the proposed Rescission was procedurally deficient under the APA because courts generally disfavor comment periods for subsequent agency actions that are shorter than the periods for the initial action and because Plaintiffs established that the shortened comment period did, in fact, cause harm.[35] Second, Judge Bush agreed with Plaintiffs that the Rescission was substantively deficient, explaining that the SEC did not make a "good-faith effort" to approximate the "costs or benefits of rescinding the 2020 Rule," since the SEC conducted only a qualitative analysis despite having access to quantitative data.[36]

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[27] *Id.* (quoting Proxy Voting Advice, 87 Fed. Reg. 43168, 43175 (July 19, 2022)).

[28] *Id.* at *6–8 (citing *Fox Television Stations, Inc.*, 556 U.S. at 516).

[29] *Id.* at *6.

[30] *Id.* at *8 (quoting *Chamber of Com.* v. *SEC*, 412 F. 3d 133, 142, 144 (D.C. Cir. 2005)).

[31] *Id.* (citing 87 Fed. Reg. at 43186, 43189).

[32] *Id.* (quoting *Chamber of Com. of U.S.*, 670 F. Supp. 3d at 555).

[33] *Id.* at *10.

[34] *Id.* at *12.

[35] *Id.* at *16–17 (Bush, J., dissenting).

[36] *Id.* at *21 (Bush, J., dissenting).

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III. Conclusion

By declining to follow *National Association of Manufacturers*—in which the Fifth Circuit concluded that the Rescission did not survive scrutiny under the APA—the Sixth Circuit has created a circuit split, not only about the legality of the Rescission, but also about broader questions about the standard for assessing legality of agency action and subsequent agency action in particular. Although neither *Chamber of Commerce of United States* nor *National Association of Manufacturers* has yet been appealed, it is possible that, given this split in authority, the Supreme Court will take up a case where it can provide guidance on the legality of agency action, particularly in light of the Supreme Court's recent decision in *Loper Bright Enterprise* v. *Raimondo*,[37] which overturned the long-standing administrative law doctrine established in *Chevron U.S.A., Inc.* v. *Natural Resources Defense Council, Inc.*[38] that, for the past 40 years, has required courts to defer to the reasonable interpretation and expertise of governmental agencies.

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to call or email authors Joel Kurtzberg (Partner) at 212.701.3120 or jkurtzberg@cahill.com; John MacGregor (Partner) at 212.701.3445 or jmacgregor@cahill.com; Jason Rozbruch (Associate) at 212.701.3750 or jrozbruch@cahill.com; Jessica Urgo (Associate) at 212.701.3882 or jurgo@cahill.com; or email publicationscommittee@cahill.com.

[37] 144 S. Ct. 2244 (2024).

[38] 467 U.S. 837 (1984).