Pearl Meyer

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Proxy Advisor Oversight Takes Center Stage This Summer

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On July 1, 2025, the US Court of Appeals for the DC Circuit resolved a long-running legal challenge to the SEC's proxy advisor rulemaking, holding that proxy voting advice does not constitute a "solicitation" under the Securities Exchange Act of 1934. Absent further appeal, the court's decision effectively halts the SEC's multi-year effort to regulate proxy advisors by subjecting their voting recommendations to the federal proxy rules. This decision was issued in the wake of a new Texas law signed into law on June 20, 2025 which regulates proxy advisors providing recommendations or other services to public companies that are headquartered or incorporated in Texas, have a principal place of business in Texas, or have proposed redomiciling to Texas.

Background of SEC Attempted Regulation

The DC Circuit Court of Appeals decision ends a six-year controversy stemming back to when the SEC issued interpretive guidance asserting that proxy voting advice may constitute a "solicitation," thereby triggering SEC proxy rules, including antifraud provisions and certain filing requirements. Institutional Shareholder Services Inc. (ISS) filed suit shortly thereafter, arguing that its voting advice is not a solicitation under the Exchange Act.

In 2020, the SEC codified its interpretive position in new rules, requiring proxy advisors to disclose conflicts of interest and to adopt policies to disseminate recommendations to issuers and notify clients of issuer responses. These rules were later softened in 2022 under then-SEC Chair Gary Gensler, with the SEC rescinding the requirement that proxy advisors share recommendations with issuers and inform clients of company responses. Nonetheless, the SEC maintained its position that proxy advice is a "solicitation," prompting ISS to renew its legal challenge.

The DC District Court granted summary judgment in favor of ISS in 2023, concluding that disinterested advice does not fall within the definition of a solicitation, with an appeal following from the SEC. On July 1, 2025, the DC Circuit held that proxy voting advice does not constitute a solicitation under the Exchange Act. The court emphasized that proxy advisors do not seek voting authority or act on behalf of issuers or shareholders, but rather offer recommendations requested by their clients. The court declined to stretch the term "solicit" to include disinterested voting advice and found no support in the statutory text or proxy rules to justify the SEC's expanded interpretation. Consequently, the SEC's 2020 Rules were deemed unlawful, and the agency's longstanding regulatory initiative was brought to an end.

State-Level Developments: Texas Enacts Proxy Advisor Legislation

On June 20, 2025, Texas enacted Senate Bill 2337, creating new state-level disclosure obligations for proxy advisors that provide services to Texas-based public companies. The legislation is the first of its kind and imposes significant compliance requirements, particularly where proxy advice is based on nonfinancial factors such as ESG or DEI considerations, or where recommendations are in conflict with the recommendations of a company's board.

Key provisions include:

Financial Interest Disclosure Requirements

Proxy advisors are subject to enhanced disclosure obligations when issuing voting advice that is *not solely in the financial interest of shareholders*, including the following:

- **Detail the Rationale**: Clearly and specifically explain the basis of the recommendation and acknowledge that the advice *prioritizes nonfinancial objectives* over shareholder financial returns, even where doing so could reduce investment performance or increase risk.
- **Prominent Notice**: Include a conspicuous statement that the advice is *not* based solely on shareholders' financial interests, due to reliance on one or more nonfinancial factors.
- **Immediate Company Notification**: Promptly send notice of such advice to the company that is the subject of the recommendation.
- **Website Disclosure**: Publicly and conspicuously disclose on the proxy advisor's website that its services are not exclusively premised on shareholder financial interests.

These obligations collectively comprise the **Financial Interest Disclosure Requirements**. Notably, the statute defines several types of advice as not financially grounded, including: (i) recommendations based wholly or partially on ESG/DEI objectives, sustainability metrics, or organizational commitments to such initiatives; and (ii) recommendations against management on shareholder proposals that *lack a Written Economic Analysis* (defined below).

"Materially Different" Disclosure Requirements

Separate and additional requirements apply where a proxy advisor provides a recommendation that is *materially different* from the company's own—unless the client has specifically requested advice based on nonfinancial considerations.

In these cases, the proxy advisor must:

- **Comply** with the **Financial Interest Disclosure Requirements**;
- **Notify** all recipients of the advice, the company, and the Texas Attorney General;
- **Clarify** whether the recommendation is based solely on financial interests; and
- **Disclose** any specific financial analysis supporting the recommendation.

This **Materially Different Disclosure** obligation also applies if a proxy advisor issues conflicting advice to different clients—unless each client has expressly sought voting advice for nonfinancial purposes.

Shareholder Proposal Disclosure Requirements

Where a proxy advisor recommends voting against a company's position on a shareholder proposal, such advice will not be deemed as based solely on financial interest *unless* it is accompanied by a **Written Economic Analysis**. That analysis must include:

- A cost-benefit assessment (short- and long-term) of implementing the proposal;
- A determination of consistency with the client's investment goals and policies;
- Projected, quantifiable impacts on investment performance if the proposal is adopted;

and
- A description of the methodology and process used to prepare the analysis.

Such recommendations must also comply with the **Materially Different Disclosure Requirements** outlined above.

The Texas law is expected to impose new operational burdens on proxy advisors, potentially limiting the services they provide to Texas-based issuers and will go into effect on September 1, 2025. Legislative efforts in Florida, Oklahoma, and West Virginia remain in early stages but may follow Texas's lead.

Pearl Meyer Observation: It will be meaningfully more expensive for proxy advisors to provide this advice in Texas, and to the extent proxy advisor clients are unwilling to bear this additional cost, we may see fewer recommendations against companies headquartered or organized in Texas. In turn, many companies may look to reincorporate in Texas or other states with similar legislation on the horizon. The Texas law may also have a chilling effect on ESG- and DEI-driven advice, with investors adjusting their proxy voting policies to focus more narrowly on financial outcomes. And perhaps the most chaotic outcome of all could be a completely fragmented proxy advisory landscape where advice varies not just by client preference but by state jurisdiction.

Looking Ahead

With the SEC's proxy advisor rulemaking effort now effectively blocked, and growing political pressure to curb the influence of proxy advisors—especially where ESG or DEI is involved—regulatory momentum is shifting to the states and potentially to Congress. Federal proposals under consideration would impose antifraud liability, conflict prohibitions, and SEC registration requirements. All such efforts are likely to face legal challenge, with the landscape expected to shift throughout the end of the year. In fact, four days after the Texas law went into effect, Glass Lewis and ISS sued Texas Attorney General Ken Paxton to block the new law, claiming it was unconstitutional and undermined their First Amendment right to advise clients even if the state didn't like the advice. We will continue to monitor both state and federal developments in this evolving regulatory environment.

About the Author

Deborah Lifshey is a managing director at Pearl Meyer, where she specializes in advising clients on compensation matters from a legal perspective including securities disclosure, taxation and corporate governance issues, negotiation contracts, and reasonableness opinion letters.

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