

# STA Newsletter

April 2010

The Securities Transfer Association, Inc.

A PUBLICATION OF THE SECURITIES TRANSFER INDUSTRY

Established 1911

## SEC Proxy Concept Release Expected: Transparency & Access Likely Targets

By T. L. Montrone

*“The only way real change to the proxy mechanics will occur is if issuers take the time and effort to prepare thoughtful responses to the SEC release.”*

The current proxy system gives brokers the obligation to distribute proxy materials to beneficial holders, while holding issuers accountable for reimbursing “reasonable” fees. Reasonable can be interpreted as anything the street wants to charge issuers. This system creates an artificial barrier between issuers and beneficial shareholders, increasing solicitation costs and making it much more difficult for issuers to communicate with their beneficial shareholders. The system also has a number of other serious deficiencies that have been ignored by both regulators and legislators. We expect the SEC to issue a White Paper or Concept Release on the proxy mechanics in the coming months. Among other things, we believe the paper will seek guidance to change the system to permit “Access”, including shareholder nominated directors on the issuers’ ballot, and to consider changes to the proxy mechanics. While the Financial Regulatory Bill sponsored by Senator Dodd contained “Access” as a proposed law, some resistance is being noted from across the aisle. Nonetheless, Access has been on the SEC list of considerations for some time and remains a likely action item.

Issuers will finally have an opportunity to weigh in on how the proxy system should work. It is essential for issuers to prepare and submit their own thoughts and comments when this SEC paper is released. The street, well funded and interested in maintaining its highly profitable, non-contractual status quo, will undoubtedly muster a mountain of specious arguments and “facts” for the current system. ***The only way real change to the proxy mechanics will occur is if issuers take the time and effort to prepare thoughtful responses to the SEC release. Issuers will continue to pay too much, not be able to recognize beneficial holders and struggle with a non-contractual arrangement unless they take the time and effort to let the SEC hear their concerns.***

With this in mind, we have provided an outline of some of the concerns issuers may want to voice in their response to the SEC release:

1. The Current Street Proxy Process is Opaque: Issuers and Beneficial Holders have no way of knowing whose vote has been counted or if it was recorded correctly. These parties cannot inquire as to the status of their vote with the tabulator. Retail beneficial holders frequently present proxies at the shareholder meeting, only to have these votes discarded, as they cannot be recognized as holders. Retail shareholders rarely understand the current NOBO/OBO definitions and are often defaulted into OBO status.
2. Beneficial shareholder voting Rights are abused through dilution – the over-distribution of Voting Instruction Forms to beneficial owners – and through the discarding of legitimate votes. Many brokers do not pre-reconcile the shareholder meeting record date position to the actual beneficial voting rights attributable to the broker’s stock position. This results in excessive voting rights being distributed. Essentially, more shares are shown in accounts than there are shares actually in the broker’s position due to stock loans or trade failures. When this process was visible to tabulators, a survey of 341 meetings revealed that over-voting occurred in **every** meeting. Under the current system, most brokers employ an “over-voting service” to advise them when more votes have been received than there are shares in position (“over-voting”). The over-voting service now alerts brokers, enabling them to discard votes without regard to validity, disenfranchising potentially legitimate votes.

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# STA Meets with SEC Chairman Mary Shapiro

*By Cynthia Jones*

On Friday, February 12, 2010, representatives from the STA met with SEC Chairman Mary Shapiro and others from the Division of Trading and Markets. In attendance from the STA were Tom Montrone, STA Vice President and Assistant Secretary, and President and CEO of Registrar and Transfer Company, Steven Nelson, STA Secretary, and Chairman and President of Continental Stock Transfer & Trust Co. and Ed Pittman, STA Counsel from Dechert LLP. The SEC group included Jamie Brigagliano, Deputy Director, Brian Bussey, Associate Director and Susan Petersen, Special Counsel for Trading and Markets. A larger group from the STA was originally planned but the extreme snowfall in various parts of the country during that week made travel impossible for some.

After a brief introduction so that the SEC staff could better understand the role of the STA, there were three topics of discussion:

- STA's petition regarding DTCC's request for rulemaking
- Proxy reform
- Trading and settlement issues affecting non exchange listed securities

Our STA representatives at the meeting felt that Chairman Shapiro understood the issues presented on all of these topics and were encouraged to believe that we are making some headway with these issues. Although nothing specific was promised at the meeting, the STA is working to set up additional discussions with DTC about the trading and settlement issues, and the SEC has promised they will attend. On the proxy front, we know that a Concept Release is circulating internally at the SEC and we expect that it will explore the issues that have been a burden to transfer agents and issuers. We will keep our membership advised of further progress. ■

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3. Distribution of proxy materials to street holders is delayed and not responsive to issuers, making solicitation not timely and expensive. The mailing typically takes place 5 to 7 business days after the registered mailing and the issuer does not have direct control over the process. Issuers cannot quickly and inexpensively conduct additional voting solicitations. Under the revised NYSE Rule 452 and with the advent of proxy access, issuers will have a greater need to communicate directly and quickly with their retail beneficial shareholders.
4. Street distribution fees are abusive, in part set without oversight, without contracts or competition and result in fees that are in excess of those charged in a competitive market. These are excessively expensive and burdensome to small companies. Companies have no choice, but must pay the amount demanded or face not being able to hold their legally required shareholder meetings. Issuers do not receive full postal discounts and cannot negotiate this or any other charges.
5. Beneficial voting is not balanced to the registered shareholders outstanding. In a

proxy contest, over votes and the inability to balance and recognize beneficial shareholders has resulted in these votes being discarded. This has directly reversed the outcome of meetings in some instances. Courts are forced to concede that beneficial holders may lose their voting rights as a result of their status as beneficial holders under the current opaque system.

### Alternative System

The street proxy mechanics should be amended to require that brokers and banks provide the issuer with a reconciled list of shareholder positions as of the meeting record date for voting purposes. Shareholders wishing confidentiality can either use a nominee position or otherwise receive their material directly from the broker at their own expense and vote through the broker's name. This is a procedure that already exists and works well in Europe. A centralized service, such as DTC, could act as an intermediary between the street and the issuer or issuer's designated agent. Cost and service would be competitive. Confidentiality laws already exist prohibiting the inappropriate distribution of shareholder information. ■