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July 30, 2019

Anne Sheehan  
Chair  
Investor Advisory Committee  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, D.C. 20549

Subject: Proxy Plumbing Recommendations  
SEC Investor Advisory Committee, File No. 265-28

Dear Ms. Sheehan:

As the SEC Investor Advisory Committee develops recommendations to improve the U.S. proxy system, please consider the attached comment letter from the Shareholder Communications Coalition, representing the issuer community.

This comment letter was submitted to the SEC earlier this year, in response to Chairman Clayton's request for recommendations regarding interim and actionable improvements to the U.S. proxy system.

Sincerely,

A handwritten signature in black ink that reads "Niels Holch". The signature is fluid and cursive, with the first name "Niels" and last name "Holch" clearly distinguishable.

Niels Holch  
Executive Director  
Shareholder Communications Coalition

Attachment

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April 8, 2019

Ms. Vanessa Countryman  
Acting Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, D.C. 20549

Subject: Recommendations for Interim Improvements to the U.S. Proxy System  
SEC File No. 4-725

Dear Ms. Countryman:

On behalf of the Shareholder Communications Coalition ([www.shareholdercoalition.com](http://www.shareholdercoalition.com)), this letter responds to the recent request by Chairman Clayton for recommendations regarding interim and actionable improvements to the U.S. proxy system.<sup>1</sup>

As the Securities and Exchange Commission ("SEC") is well aware, the U.S. proxy distribution and voting system is bifurcated between registered shareholders and "street name" shareholders of a public company, largely as a result of regulations promulgated in the 1980's.

Under current SEC rules, public companies can communicate directly with their registered shareholders, which typically comprise about 25% of their shareholder base. Registered shareholders appear on each company's stock ledger. Companies are permitted to disseminate proxy statements to their registered shareholders without the assistance of financial intermediaries and these shareholders receive a proxy card for voting their shares. Registered shareholders return their proxy cards back to the official tabulator for the election and, if they so choose, can use their legal proxy to attend a shareholder meeting in person.

For the remaining shareholders, who hold their shares in street name, the process works differently. Public companies distribute proxy materials and otherwise communicate with these shareholders through the brokers and banks that hold their shares in nominee form. A central intermediary, representing the substantial majority of brokers and banks, handles all proxy distribution activities and shareholder communications. This intermediary is compensated through a fee schedule developed and approved by the national securities exchanges. Street

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<sup>1</sup> See *infra* notes 5 and 6.

name shareholders—also called beneficial owners—receive proxy materials and voting instruction forms (“VIFs”) and return voting instructions to the central intermediary for each shareholder meeting. A shareholder interested in attending a shareholder meeting in person must secure a legal proxy from the broker or bank holding his or her shares.

For many decades, U.S. public companies have sought access to contact information for all of their beneficial owners, for the purpose of engaging in direct communications with them.<sup>2</sup> These companies have requested changes to SEC rules that would: (1) eliminate the Non-Objecting/Objecting Beneficial Owner classification system (“NOBO/OBO”) embedded in the Commission’s rules; and (2) provide each public company with a list of its beneficial owners, upon request and for a reasonable fee.<sup>3</sup>

Public companies would like the option to choose their own service providers when distributing proxy materials and disseminating other communications to their shareholders. They also would like to see improvements made to the proxy voting process, to ensure that it is fully transparent and verifiable. Two of the more urgent improvements that should be made are: (1) starting the proxy process with a fully reconciled list of beneficial owners eligible to vote at a shareholder meeting; and (2) reducing the bifurcation in the voting system by permitting beneficial owners to cast votes using legal proxies, instead of voting instruction forms.

On November 15, 2018, the SEC staff held a Roundtable on the Proxy Process.<sup>4</sup> Several weeks later, Chairman Clayton announced that a Commission initiative in 2019 would be to improve the proxy process.<sup>5</sup> In his remarks, Chairman Clayton acknowledged that a major overhaul of the proxy system could take time. He requested that proxy process participants provide comments to the Commission about what can be done in the interim to improve the current system.<sup>6</sup>

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<sup>2</sup> See, e.g., Securities and Exchange Commission, Final Report on the Practice of Recording the Ownership of Securities in the Records of the Issuer in Other Than the Name of the Beneficial Owner of Such Securities, at 37 (1976) (hereinafter “SEC Street Name Study”) (“Support for this approach came from a number of issuers who believe that the advantages of full disclosure of beneficial ownership and direct issuer-shareholder communications outweigh the impact of this approach on the securities transaction processing system and on the operations of brokers, banks and issuers.”); and Advisory Committee on Shareholder Communications, Improving Communications Between Issuers and Beneficial Owners of Nominee Held Securities, at 54 (1982) (hereinafter “SEC Advisory Committee Report”) (“It has long been asserted that corporate-shareholder communications would improve demonstrably if issuers were provided with the identities of beneficial owners for the purpose of directly communicating with them.”).

<sup>3</sup> See, e.g., Letter from Niels Holch, Executive Director, Shareholder Communications Coalition, to The Honorable Mary L. Schapiro, Chairman, U.S. Securities and Exchange Commission (Aug. 4, 2009), *available at* <https://www.sec.gov/comments/s7-14-10/s71410-3.pdf>.

<sup>4</sup> See Spotlight on Proxy Process, November 15, 2018: Roundtable on the Proxy Process, <https://www.sec.gov/proxy-roundtable-2018> (last visited Mar. 26, 2019).

<sup>5</sup> Jay Clayton, Chairman, Securities and Exchange Commission, SEC Rulemaking Over the Past Year, the Road Ahead and Challenges Posed by Brexit, LIBOR Transition and Cybersecurity Risks (Dec. 6, 2018).

<sup>6</sup> *Id.* (“I encourage all those interested in improving the proxy plumbing to share their thoughts, particularly regarding actionable, interim improvements.”).

In response to this request for recommendations, what follows are several immediate and interim regulatory actions the SEC can take, on a pathway to a proxy system that permits direct shareholder communications and an improved beneficial owner voting process:

1. **Expand the Use of the NOBO List.** Under current SEC rules, brokers and banks are required to classify each street name shareholder as either a Non-Objecting Beneficial Owner (“NOBO”) or as an Objecting Beneficial Owner (“OBO”), for shareholder communications purposes. This classification is typically made based on indications by a beneficial owner at the time they open an account with the intermediary.

The names of OBOs may not be disclosed by brokers and banks to a public company for any purpose whatsoever. The names of NOBOs may be disclosed to a company for the purpose of sending an annual report, or to engage in general “corporate communications.”<sup>7</sup> A NOBO list can be obtained at any time by a company and not only in connection with a shareholder meeting.<sup>8</sup> However, current SEC rules do not permit public companies to disseminate proxy materials to NOBOs.

The restriction on public company distribution of proxy materials dates back to the 1980’s. An SEC Advisory Committee Report in 1982 did consider whether to permit public companies to disseminate proxy materials to non-objecting beneficial owners.<sup>9</sup> However, the Advisory Committee did not recommend this approach primarily because public companies were not in a position in 1982 to assimilate lists of beneficial owners holding street name shares on a record date from hundreds of brokers and banks.<sup>10</sup>

This technical problem was resolved in 1985, with the selection of a central intermediary—the Independent Election Corporation of America—to compile and supply beneficial owner lists from the approximately 900 brokers and banks holding shares in nominee form.<sup>11</sup>

Without these technical obstacles, it makes little sense for SEC rules to permit a

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<sup>7</sup> See, e.g., 17 CFR 240.14a-13(b)(4) and 240.14a-13(c); 17 CFR 240.14b-1(b)(3); 17 CFR 240.14b-2(b)(4)(ii); and 17 CFR 240.14c-7(b)(4) and 240.14c-7(c).

<sup>8</sup> See, e.g., Facilitating Shareholder Communications, 1985 SEC LEXIS 530, at 28-29 (October 15, 1985) (hereinafter “1985 SEC Final Rule”) (“Because these rules are intended to provide for maximum communication between registrants and their beneficial owners, the Commission is of the view that, at this time, registrants should not have limits imposed on the number of requests for beneficial owner lists and, accordingly, has not adopted any such limits.”).

<sup>9</sup> See SEC Advisory Committee Report at 58-60.

<sup>10</sup> *Id.* at 62.

<sup>11</sup> 1985 SEC Final Rule at 8 (October 15, 1985) (“The Ad Hoc Committee [on Identification of Beneficial Owners] requested proposals and selected Independent Election Corporation of America (‘IECA’) to serve as the intermediary between registrants and brokers in supplying lists of beneficial owners.”).

public company to disseminate an annual report to a list of NOBOs without also sending the proxy materials that should accompany it. Annual reports contain important information necessary to make an informed voting decision and there is no need to bifurcate the proxy distribution process for street name shareholders who are classified as NOBOs.

As an interim step to a more direct shareholder communications system, SEC rules should be amended to permit public companies to distribute proxy materials to NOBOs, in advance of a shareholder meeting.<sup>12</sup> NOBO lists should be provided electronically, for ease in processing; and a beneficial owner's contact information should include his or her mailing address, email address (where available), and delivery preferences.

2. **Require Pre-Mailing Reconciliation of Beneficial Owner Positions.** As noted in the SEC's 2010 Concept Release on the U.S. Proxy System ("2010 Concept Release"), brokers and banks hold many of their securities in book-entry form through the Depository Trust Company ("DTC"), a registered clearing agency acting as a securities depository.<sup>13</sup> These securities are held in "fungible bulk," meaning that there are no specifically identifiable shares directly owned by each broker or bank that is a DTC participant.

An imbalance in beneficial owner voting can occur as a result of current share lending practices by brokers and other intermediaries. Share lending enables a "short" investor to borrow shares from a "long" investor, with an agreement to return these borrowed shares at a later date.<sup>14</sup> Share lending agreements generally assign voting rights to whomever possesses the shares on a company's record date, causing the need for each intermediary to reconcile its long and short positions to accurately calculate the number of shares each beneficial owner is entitled to vote.<sup>15</sup>

Absent a reconciliation process *before* proxy materials are disseminated, a broker may be submitting more votes at the beneficial owner level than it is entitled to vote. Equally of concern, a lack of pre-mailing reconciliation results in proxy materials and VIFs being sent to beneficial owners who are not legally eligible to vote.

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<sup>12</sup> A public company requesting a NOBO list would pay the charges listed on the current NYSE fee schedule approved by the SEC. The charges for providing beneficial ownership information to companies currently are: (1) 6.5 cents for each NOBO name; and (2) an agent processing fee of between 4-10 cents per name, based on a sliding scale. See NYSE Rule 451.92 and NYSE Rule 465, *available at*

[http://wallstreet.cch.com/nvsetools/PlatformViewer.asp?SelectedNode=chp\\_1\\_6&manual=/nyse/rules/nyse-rules/](http://wallstreet.cch.com/nvsetools/PlatformViewer.asp?SelectedNode=chp_1_6&manual=/nyse/rules/nyse-rules/).

<sup>13</sup> Concept Release on the U.S. Proxy System, 75 Fed. Reg. 42,982, at 42,986 (July 22, 2010).

<sup>14</sup> Many individual investors with margin accounts do not realize that standard account agreements permit the broker to loan out their securities, or remove securities to avoid a fail-to-deliver problem at settlement, without notice. Proxy materials and VIFs can be sent to retail investors who are not aware that they don't actually possess the shares in their account and, therefore, are not eligible to vote as of a company's record date.

<sup>15</sup> A need also exists to reconcile voting imbalances that can occur when another broker has failed to deliver a security on a timely basis, yet a customer's account has been credited with the security as of settlement date. This can cause an overvote at the beneficial owner level, absent an appropriate reconciliation as of a company's record date. See SEC Staff Briefing: Roundtable on Proxy Mechanics, at 1-2 (May 24, 2007).

This problem of overvoting at the beneficial owner level has been an issue for a number of years. In 2006, the New York Stock Exchange (“NYSE”) sanctioned four brokers for failing to reconcile their beneficial ownership positions in a timely manner to avoid over-voting at shareholder meetings.<sup>16</sup>

As a result of these NYSE administrative proceedings, the securities industry adopted written guidelines to address this reconciliation problem.<sup>17</sup> These guidelines permit brokers to select one of two reconciliation methods. Under the first method—called pre-mailing reconciliation—a broker reconciles its long positions with its share lending positions (and failure to deliver positions) *before* a proxy mailing takes place, so that proxy materials are only sent to customer positions authorized to vote in a shareholder meeting.

Under the second method—called post-mailing reconciliation—a broker compares its aggregate position at DTC (and with other depositories) with its actual aggregate customer account positions only after receiving VIFs back from its customers and during the vote tabulation process.

The pre-mailing reconciliation method ensures that only those shareholders who are legally eligible to vote at a shareholder meeting are the ones actually voting. Post-mailing reconciliation is an after the fact remedy that permits low response rates by retail investors to obscure share lending positions and failure to deliver problems within each broker’s aggregate share position at DTC. When a post-mailing reconciliation is required, certain beneficial owners are disenfranchised by the allocation decisions that are made by a broker when it needs to adjust the number of beneficial owner votes that are cast down to the level of shares in its aggregate DTC position.

The securities industry guidelines that provide two methods of beneficial owner reconciliation should be replaced with an SEC rule that requires pre-mailing reconciliation as the only method for brokers and other intermediaries. Street name positions should be reconciled as of the record date for each shareholder meeting, in order to avoid discrepancies in tabulating

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<sup>16</sup> See *In the Matter of Deutsche Bank Securities, Inc.*, Request for Review of Exchange Hearing Panel Decision 05-45, NYSE Board of Directors (Feb. 2, 2006), available at <https://www.nyse.com/publicdocs/nyse/markets/nyse/disciplinary-actions/2006/05-045.pdf>; *Credit Suisse Securities USA) LLC*, NYSE Hearing Panel Decision 06-54 (Apr. 18, 2006), available at <https://www.nyse.com/publicdocs/nyse/markets/nyse/disciplinary-actions/2006/06-054.pdf>; *UBS Securities LLC*, NYSE Hearing Panel Decision 06-55 (Apr. 18, 2006), available at <https://www.nyse.com/publicdocs/nyse/markets/nyse/disciplinary-actions/2006/06-055.pdf>; and *Goldman Sachs Execution & Clearing, L.P.*, NYSE Hearing Board Decision 06-61 (May 4, 2006), available at <https://www.nyse.com/publicdocs/nyse/markets/nyse/disciplinary-actions/2006/06-061.pdf>.

<sup>17</sup> Securities Industry Association, *Suggested Practice Guidelines for Proxy Processing*, Sept. 2006, available at <http://www.shareholdercoalition.com/sites/default/files/SIA%20ProxyGuidelinesSep2006.pdf>.

final vote counts and to avoid distributing proxy materials to beneficial owners who are ineligible to vote.

3. **Ensure that NOBO is the Default Position.** There is a lack of uniformity among brokers and banks regarding how beneficial owners are actually classified as NOBOs or OBOs. There are no formal standards or regulatory rules requiring a broker or bank to follow: (a) a particular process or procedure for reviewing this NOBO/OBO classification with its customers at account opening, or (b) any procedure or timeline for updating this classification on a periodic basis.

When the NOBO/OBO rules were adopted in 1983, the SEC specifically rejected a requirement that each beneficial owner provide affirmative consent to be classified as a NOBO.<sup>18</sup> Instead, the Commission sought to encourage more robust shareholder communications by choosing a non-objection standard for the disclosure of beneficial owner information to companies.<sup>19</sup>

The SEC final rule left to the discretion of brokers how to ascertain whether a particular beneficial owner objects to disclosure.<sup>20</sup> It also permitted companies to be able to communicate with their beneficial owners about the benefits of direct communications resulting from being classified as a NOBO.<sup>21</sup>

Historical studies on this issue have observed that most retail investors do not object to having their identity disclosed to the companies in which they are invested as shareholders. In the 1976 Street Name Study by the SEC, a survey of more than 97,000 beneficial owners indicated that only 12 percent of those holding in street name would object to disclosure of their identity to a public company for purposes of direct communication.<sup>22</sup> The remaining 88 percent indicated that they would not object to such disclosure.<sup>23</sup>

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<sup>18</sup> See Facilitating Shareholder Communications Provisions, 1983 SEC LEXIS 1151 (July 28, 1983), at 16-17 (“The Commission believes that such a [non-objection] standard best facilitates shareholder communications by encouraging the greatest participation of shareholders whose securities are held in nominee name. At the same time, the Commission believes (sic) that privacy concerns are adequately addressed by giving beneficial owners an opportunity to object to disclosure.”).

<sup>19</sup> *Id.*

<sup>20</sup> *Id.* at 18 (“The Commission agrees that it is appropriate to leave to brokers’ discretion the way in which they communicate with their customers ....”).

<sup>21</sup> *Id.* at Note 15 (“Commentators requested that issuers be permitted to prepare letters to be sent to beneficial owners as a means for issuers to inform beneficial owners of the benefits of direct communication. Under current rules of the national securities exchanges brokers are required to mail to beneficial owners material sent by issuers upon assurance of reimbursement. Thus, issuers are permitted to mail to beneficial owners any communication provided they bear the cost.”).

<sup>22</sup> SEC Street Name Study at 41 (“The Commission’s survey indicates that shareowners as a group are less concerned than intermediaries about the disclosure of their names to issuers.”).

<sup>23</sup> *Id.*

Likewise, a 2006 investor survey by the NYSE found that there was significant investor confusion about the proxy voting process and the NOBO/OBO classification system.<sup>24</sup> However, the survey also found that when a comprehensive explanation of the difference between NOBO and OBO status is given, investors selected NOBO by nearly a 2-1 margin.<sup>25</sup>

The SEC can resolve this issue by following a process now being used to ascertain investor preferences regarding electronic delivery of mutual fund disclosure documents. Last June, the SEC adopted a final rule that provides investment companies with the option to shift the default for delivering shareholder reports to an electronic, web-based method.<sup>26</sup> The final rule provides for paper notices to be sent to investors about this upcoming change over a two-year period.<sup>27</sup> This two-year period permits investment companies and their intermediaries adequate time to educate investors about the coming change and permit investors who prefer to receive their reports via paper delivery the ability to express their delivery preference and maintain the status quo.<sup>28</sup>

This same type of process could be used to provide a uniform method to educate beneficial owners about the differences between being a NOBO and an OBO. A two-year period could be used to permit any investor who is an OBO to express a preference to remain in that status before any default classification shifts to NOBO. At the end of this education and notice process, any investor who has not objected to the disclosure of identity and contact information with a public company would be deemed a NOBO for proxy distribution and corporate communications purposes.

4. **Extend Omnibus Proxy Authority to the Beneficial Owner Level.** Under state law, DTC (and other depositories) serve as the actual record holder of street name shares. To transfer proxy voting authority to its participant brokers and banks, DTC created an “omnibus proxy” procedure in 1975.<sup>29</sup> This procedure was described in the SEC’s 1976 Street Name Study as follows:

Under this procedure, the depository prepares a computer generated list of the names and holdings of participants that have depository positions in an issuer’s securities as of the record date. The list is forwarded to the issuer along with an ‘omnibus proxy’ which authorizes each participant, to the extent of the participant’s position, to act as the depositor’s proxy and to vote the securities. The procedure is used today by the three major

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<sup>24</sup> Opinion Research Corporation, *Investor Attitudes Study*, at 3 (Apr. 7, 2006), *available at* [http://www.shareholdercoalition.com/sites/default/files/NYSE%20ORC%20Investor%20Study%204-7-06\\_0.pdf](http://www.shareholdercoalition.com/sites/default/files/NYSE%20ORC%20Investor%20Study%204-7-06_0.pdf).

<sup>25</sup> *Id.* at 21.

<sup>26</sup> Optional Internet Availability of Investment Company Shareholder Reports, 83 Fed. Reg. 29,158 (June 22, 2008).

<sup>27</sup> *Id.* at 29,177.

<sup>28</sup> *Id.*

<sup>29</sup> See *SEC Street Name Study* at 15.



securities depositories and has largely removed depositories from the shareholder communications process.<sup>30</sup>

As noted in the SEC's 2010 Concept Release, securities intermediaries do not typically transmit actual proxy cards to beneficial owners as a part of the proxy solicitation process. While some banks do send proxy cards to their beneficial owners, as permitted by SEC rules, brokers and many banks use the VIF system described earlier for beneficial owners to indicate their voting preferences for a shareholder meeting.<sup>31</sup> Under this process, only a broker or a bank holds proxy authority once DTC has executed an omnibus proxy.

There is no reason why brokers and banks shouldn't, in turn, execute omnibus proxies in favor of their NOBO customers who are receiving proxy materials directly from companies.<sup>32</sup> This would permit a proxy card—instead of a VIF—to accompany the proxy statement. After voting, a beneficial owner would return the proxy card to the tabulator for each shareholder meeting. The proxy card would be processed in the same manner as issuer proxies returned to the tabulator by registered shareholders.

A transfer of voting authority to the beneficial owner level eliminates the need for broker discretionary voting under NYSE Rule 452 for any NOBO receiving proxy materials directly from a public company.<sup>33</sup> However, additional steps should be taken to ensure that the loss of broker discretionary voting for these beneficial owners does not harm the ability of any public company—especially a small or mid cap issuer—to obtain a quorum at a shareholder meeting. To address this concern, conditional language should be added to the omnibus proxy instrument to authorize DTC, or another depository, to vote the shares of any unreturned proxies as “present,” for the limited purpose of establishing a quorum for the shareholder meeting.<sup>34</sup>

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Thank you for the opportunity to present these recommendations for interim improvements to the U.S. proxy system. If you have questions, or need additional information, please contact me at [REDACTED], or via email at [REDACTED].

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<sup>30</sup> *Id.*

<sup>31</sup> Banks are already permitted by SEC regulations to send legal proxies to respondent banks and beneficial owners. See 17 C.F.R. § 240.14b-2(b)(2)(i) and § 240.14b-2(b)(3)(i).

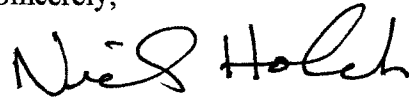
<sup>32</sup> This recommendation would be an interim step. If the NOBO/OBO classification system is eliminated in a later rulemaking, brokers and banks could issue omnibus proxies transferring proxy voting authority to all beneficial owners receiving proxy materials directly from a public company.

<sup>33</sup> Providing a legal proxy to beneficial owners also permits them to attend a shareholder meeting and vote in person without having to take the additional step of obtaining a proxy from his or her broker or bank. A VIF does not authorize a beneficial owner to vote his or her shares in person at a shareholder meeting.

<sup>34</sup> This recommendation is consistent with existing SEC rules. See 17 C.F.R. § 240.14a-4(b)(1) (“A proxy may confer discretionary authority with respect to matters as to which a choice is not specified by the security holder provided that the form of proxy states in bold-face how it is intended to vote the shares represented by the proxy in each such case.”).

Letter to Ms. Vanessa Countryman  
April 8, 2019  
Page 9

Sincerely,

A handwritten signature in black ink that reads "Niels Holch". The signature is written in a cursive style with a large, stylized "N" and "H".

Niels Holch  
Executive Director  
Shareholder Communications Coalition

cc: The Honorable Jay Clayton  
The Honorable Robert J. Jackson, Jr.  
The Honorable Hester M. Peirce  
The Honorable Elad L. Roisman  
William Hinman, Director, Division of Corporation Finance  
Dalia Blass, Director, Division of Investment Management  
Brett Redfearn, Division of Trading and Markets