THE STA
SECURITIES TRANSFER ASSOCIATION, INC.

December 17 2012

Elizabeth Murphy
Secretary
U.S. Securities and Exchange Commission
100 F St.
Washington DC 20549

Re: SEC Concept Release #34-6i2495 on the U.S. Proxy System
File Number S7-14-10

Dear Ms. Murphy:

On behalf of the STA, I am submitting for the public file the attached letter that was sent by the STA to Commissioners Paredes and Gallagher relating to the recent NYSE proxy fee proposals. We will be happy to provide any further information that you or the Commissioners might require.

Sincerely,

Cynthia Jones

Cynthia Jones
Executive Director
The Securities Transfer Association. Inc.

Enclosure

THE STA
SECURITIES TRANSFER
ASSOCIATION, INC.

December 13, 2012

The Honorable Daniel M. Gallagher
The Honorable Troy A. Paredes
Commissioners
U.S. Securities & Exchange Commission
100 F Street, NE
Washington, D.C. 20549

Re: NYSE Proposed Rule - Proxy Fees (SR-NYSE-2012-39)

Dear Commissioners Gallagher and Paredes:

On behalf of the Securities Transfer Association[1] ("STA"), I am writing to urge you to disapprove a proposal by the New York Stock Exchange ("NYSE") to amend its Rules 451 and 465, regarding the fees to be charged to issuers and shareholders involved in distributing proxy and other materials to investors holding corporate securities in "street name."[2] This rule proposal, SR-NYSE-2012-39, was filed informally with the SEC on or around September 7, 2012, but has not yet been issued for public comment as of this writing.

The NYSE proposal implements recommendations by the NYSE Proxy Fee Advisory Committee ("PFAC"), which were

[1] The Securities Transfer Association ("STA") is an industry trade association, established in 1911, comprised of transfer agents that provide services to more than 12,000 large and small public companies in the United States. The STA and its members work closely with issuers of securities on a variety of public policy matters and been active over many years in advocating for a fair and efficient system for proxy distribution and shareholder communications.

[2] Since 1937, the New York Stock Exchange ("NYSE") has determined the level of reimbursement for proxy distribution and communications activities to be provided by issuers (and other parties) to its broker-dealer members. The proxy fee schedule developed by the NYSE is used by banks and other stock exchanges for the same purpose. This fee schedule appears in NYSE Rules 451 and 465.

contained in a report issued on May 16, 2012.[3] The PFAC was formed in September 2010 to review NYSE proxy rules and their application to issuers and other stakeholders.

As you know, SEC rules require broker-dealers and banks to distribute corporate proxy materials to their customers, called beneficial owners, under the street name system.[4] The cost of distributing these materials (and communicating with beneficial owners) is the responsibility of the issuer, which is required by the same rules to reimburse broker-dealers and banks for their "reasonable" expenses.[5]

A substantial majority of broker-dealers and banks have outsourced their proxy processing responsibilities to Broadridge Financial Solutions ("Broadridge"). As an agent of, and service provider to, these broker-dealers and banks, Broadridge distributes proxy materials for annual and special meetings to beneficial owners, while transfer agents distribute proxy materials to the registered shareholders listed in their records.

Despite an 18-month effort to review the NYSE proxy fee schedule, this proposed rule change recommended by the PFAC should be disapproved because the NYSE *failed to*: (1) conduct a rigorous and independent cost/benefit analysis; (2) correct the current use of proxy processing fees outside of their intended scope; (3) examine rebates to broker-dealers from issuer invoice payments; and (4) address inappropriate charges to issuers for separately managed accounts.

The NYSE Failed to Conduct a Rigorous and Independent Cost/Benefit Analysis on this Proposed Rule

Earlier this year, both of you registered your objections to the SEC's approval of an interpretive notice by the Municipal Securities Rulemaking Board ("MSRB"), a self-regulatory organization ("SRO"). Shortly after this notice was issued, you released a joint public statement noting that approval of SRO rules should be subject to the same rigorous analysis as the Commission's own rules:

> Any rulemaking—whether by a self-regulatory organization, such as the MSRB, or by the Commission itself—should be the product of a careful and balanced assessment of the potential consequences that could arise. Such an assessment should entail a thorough analysis of both the intended benefits and the possible costs of a proposed rulemaking in order to ensure that any regulatory decision to proceed with the initiative reflects a well-reasoned conclusion that

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[3] New York Stock Exchange, Recommendations of the Proxy Fee Advisory Committee to the New York Stock Exchange, May 16, 2012, available at https://usequities.nyx.com/sites/usequities.nyx.com/files/final_pfac_report.pdf (hereinafter "NYSE PFAC Report").
[4] See 17 C.F.R. § 240.14b-1 and 17 C.F.R. § 240.14b-2.
[5] See, e.g., 17 C.F.R. § 240.14a-13(a)(5).

> the benefits will come at an acceptable cost. This requires identifying the scope and nature of the problem to be addressed, determining the likelihood that the proposed rulemaking will mitigate or remedy the problem, evaluating how the rule change could impact affected parties for better and for worse, and justifying the recommended course of action as compared to the primary alternatives.[6]

One reason that the NYSE proposed rule on proxy fees does not meet this standard is that there has *never* been an independent evaluation of actual broker-dealer costs involved in proxy distribution activities. The last large industry study was in 1986, when the NYSE conducted a survey of its broker-dealer members to determine their actual proxy costs, after the NYSE initiated a competitive bidding process for a central intermediary to compile and supply beneficial owner contact information.[7] Since that time, the NYSE has periodically reviewed its proxy fee schedule by establishing advisory panels of broker-dealers, issuers, and other proxy process participants to develop recommendations for any modifications to its rules.[8]

The NYSE advisory panel process is no longer able to evaluate what reasonable reimbursements should be for proxy services. The proxy system has become very complex, with many interdependent entities. And a great deal has happened over the past 25 years, with both the use of technology and changing investor needs in this area. The paper-based systems used by broker-dealers and other intermediaries have been replaced with very sophisticated electronic back office systems. Similarly, the distribution of proxy materials has changed dramatically, with the increased use of householding, electronic delivery of materials to investors, and the SEC's decision in 2007 to permit the Notice and Access format. Additionally, the number of street name accounts has grown over the years, as investors are choosing to hold their securities through financial intermediaries, instead of registering their shares directly.

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[6] Commissioners Daniel M. Gallagher and Troy A. Paredes, Statement Regarding Commission Approval of MSRB Rule G-17 Interpretive Notice, May 14, 2012, available at http://www.sec.gov/news/speech/2012/spch051412dmgtap.htm (hereinafter "Gallagher and Paredes Statement"). Commissioner Gallagher also expanded on this statement in remarks at SIFMA's Annual Market Structure Conference this fall. See Commissioner Daniel M. Gallagher, "Market 2012: Time for a Fresh Look at Equity Market Structure and Self-Regulation," October 4, 2012, available at http://www.sec.gov/news/speech/2012/spch100412dmg.htm ("The Commission's 19(b) review process for SRO rule filings is not meant to be a rubber stamp for proposed new SRO rules, and the Commission's delegation of authority to staff to review those filings cannot be an abdication of its responsibilities to ensure that SRO rule proposals are fully vetted and pass legal muster. … If self-regulation is to continue to play a central role in securities regulation, SROs must be committed to ensuring that the rules they send to the Commission for approval are the result of the same degree of rigorous analysis as the Commission applies to its own rules.").

[7] See SEC Release No. 34-22889, 51 Fed. Reg. 5,821, at 3 (Feb. 18, 1986); and SEC Release No. 34-22533, 50 Fed. Reg. 42,672, at 4 (Oct. 22, 1985).

[8] NYSE PFAC Report at 7-8.

The PFAC review of the NYSE proxy fee schedule took 18 months and involved 12 individuals hand-picked by the NYSE to receive testimony and review written comments from a number of participants in the proxy process. However, the final PFAC report and recommendations rely almost exclusively on data provided by Broadridge, which enjoys a near-monopoly in providing these proxy services to broker-dealers and banks.

Very little information or analysis in the PFAC report was provided by independent sources or by industry organizations.[9] As an example, the STA has issued two cost studies of its own over the past two years, comparing Broadridge and transfer agent pricing for the same proxy services.[10] Neither of these studies was even mentioned in the PFAC report, despite the fact that both STA studies concluded that issuers are being overcharged by more than 40% by broker-dealers and Broadridge for proxy services.

The NYSE's approach on proxy fees needs to change. And the only method by which the NYSE can obtain accurate cost information about proxy processing activities is through the use of an independent third-party, one which is without the conflicts that exist between Broadridge and its clients.[11] The use of an independent third-party for this purpose was strongly recommended by the previous NYSE Proxy Working Group[12] in a report issued in 2006:

> The Proxy Working Group therefore recommends that the NYSE should periodically re-evaluate the fees structure to ensure that no entity is unduly profiting off the current system. Issuers and shareholders deserve periodic confirmation that the system is performing as cost-effectively, efficiently and accurately as possible, with the proper level of responsibility and accountability in the system.
>
> To achieve these objectives, the Proxy Working Group recommends that the NYSE engage an independent third party to analyze what is a 'reasonable' amount for issuers to be charged pursuant to Rule 465

[9] As an example, more than 25% of the footnotes in the PFAC Report cite and rely on data provided solely by Broadridge. Only 3 of 38 footnotes rely on information developed by outside third parties. The balance of the footnotes cite SEC and NYSE sources.
[10] See, infra, note 18.
[11] As an example, the PFAC report relies in part on a representative survey by SIFMA of only 15 broker-dealers to develop industry cost data for analysis by the PFAC members. Instead of an approach in which a limited number of broker-dealers participate in a general survey, the NYSE should be conducting a more robust and independent cost evaluation. See Letter from Tom Price, Managing Director, Operations, Technology, & BCP, SIFMA, to Judy McLevey, Vice President, NYSE Euronext, May 30, 2012.
[12] The NYSE Proxy Working Group was created in April 2005 and chaired by Larry W. Sonsini, Chairman of Wilson Sonsini Goodrich & Rosati.

> and to conduct cost studies of the current services provided by [Broadridge] and commission an audit of [Broadridge] costs and revenues for proxy mailing. These studies and audit should include a detailed review of [Broadridge's] actual and anticipated future costs, especially in light of the new electronic delivery proposal by the SEC. The NYSE should disclose the findings of these regular reviews to a Sub-Committee of the Working Group before instituting any changes to the current fees.
>
> The Working Group also recommends that the NYSE review [Broadridge's] contract arrangements with brokers. It is understood that these contracts are designed to cover the brokers' costs of providing information about beneficial owners to [Broadridge], but since the reimbursement is tied to the fees regulated by the NYSE, they should be carefully reviewed to make sure that these agreements are not covering other costs unrelated to beneficial owner information.[13]

The NYSE should be required to follow this recommendation by its Proxy Working Group to engage an independent third-party to evaluate the structure and level of fees being paid for proxy distribution and shareholder communications services. This independent evaluation should include a review of broker-dealer and bank contracts with their proxy service providers, to ensure that these agreements do not include activities not directly related to the proxy process.

<u>The NYSE Rule Proposal Failed to Correct the Current Use of Proxy Processing Fees Outside of Their Intended Scope</u>

The basic processing fee, which currently ranges between $0.45 and $0.50 per beneficial owner position (including an intermediary unit fee), was originally intended to be charged for processing activities necessary to prepare and mail a physical proxy package to a beneficial owner. These fees were designed to reimburse for the printing of a Voting Instruction Form ("VIF") and enclosing it with an issuer's annual report, proxy statement, and return envelope in a poly-wrapped package for mailing. However, this fee is now being charged for all shareholder positions, even where no packages are being mailed, or—in the case of separately managed accounts—where the beneficial owner does not receive any proxy materials at all.[14]

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[13] New York Stock Exchange, <u>Report and Recommendations of the Proxy Working Group to the New York Stock Exchange</u>, at 28, June 5, 2006, available at http://www.nyse.com/pdfs/REVISED_NYSE_Report_6_5_06.pdf.

[14] The processing fees charged by Broadridge also include costs for print communications services, and Broadridge does not reduce this fee for positions that do not require paper communications services. Moreover, and as discussed below, Broadridge and its broker-dealer clients charge issuers for separately managed accounts, where proxy voting has been delegated to an investment adviser and no proxy materials

A second fee, called the paper and postage elimination fee, is charged for suppressing the need to mail proxy materials to certain beneficial owner positions, such as when householding is used and/or when an investor chooses electronic delivery. This suppression fee, which ranges from $0.25 to $0.50, was originally intended to be an incentive fee for converting beneficial owners to electronic delivery. However, this fee is always treated as an "evergreen" fee, charged both in the first year an election is made and also in each year thereafter.[15]

This suppression fee issue was raised and discussed in the 2010 SEC Concept Release on the U.S. Proxy System.[16] Instead of addressing this problem, the PFAC report attempts to transform this fee into a new purpose, calling it a "preference management fee," without any evaluation of what suppression activities are actually involved, the cost of those activities, and whether issuers should be responsible for these activities, especially on an ongoing basis.

Additionally, the PFAC failed to study the inter-relationship between suppression fees and the basic processing fees also charged for these positions. If Broadridge is to be paid a "preference management fee" to track shareholder preferences regarding householding or electronic delivery, then why is it necessary for issuers to also pay for a basic processing fee (and an intermediary unit fee) for positions that are suppressed?

A third fee, affecting issuers using the Notice and Access format, ranges from $0.05 to $0.25 for each beneficial owner position. These fees are not currently included in the NYSE proxy fee schedule. Notice and Access fees are applied on top of the basic processing fees, even though there are significantly lower costs to process a one-page mailing and deliver proxy materials electronically, compared to mailing a full proxy package. This is another area which would benefit from a cost study by an independent third party.

Without any evaluation or discussion of the actual costs of providing these services, the PFAC recommends that Notice and Access fees be included in the NYSE fee schedule at their current levels. Despite issuer concerns that Broadridge charges these fees for all account positions holding an issuer's shares—including those that are already suppressed—the PFAC decided not to change any Broadridge practices involving these fees.

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are distributed at the beneficial owner level. In addition to practices in assessing processing fees that do not reflect actual costs, Broadridge derives surplus revenue from postage by charging mailing rates that are higher than actual postage costs.

[15] These suppression fees also have a print communications component to them and, similar to the processing fees noted above, Broadridge does not reduce these fees for positions that do not require any print communications services.

[16] Concept Release on the U.S. Proxy System, 75 Fed. Reg. 42,982, at 42,997 (July 22, 2010) (hereinafter "SEC Concept Release").

The NYSE Rule Proposal Failed to Examine Rebates to Broker-Dealers from Issuer Invoice Payments

It is widely known that broker-dealers are receiving rebates from Broadridge for proxy processing activities. It is also believed that broker-dealers may be receiving services from Broadridge that are outside the scope of the proxy process and are being paid for by issuer payments based on the NYSE proxy fee schedule. This issue was discussed in the SEC's 2010 Concept Release on the U.S. Proxy System:

> It is our understanding that Broadridge currently bills issuers, on behalf of its broker-dealer clients, the maximum fees allowed by NYSE Rule 465. However, we understand that the fees Broadridge charges its largest broker-dealer clients for its services sometimes are less than the maximum NYSE fees charged to issuers on the broker-dealers' behalf, resulting in funds being remitted from Broadridge to a subset of its broker-dealer clients. This practice raises the question as to whether the fees in the NYSE schedule currently reflect 'reasonable reimbursement.' While the issuer pays the proxy distribution fees, the issuer has little to no control over the process by which the proxy service provider is selected, the terms of the contract between the broker-dealer and the proxy service provider, or the fees that are incurred through the proxy distribution process.[17]

Proxy fees are intended to be reimbursement for reasonable expenses. Fees should be based on actual costs and not used to fund "back office" services that benefit only Broadridge and its clients.

As noted earlier, the STA has conducted two cost studies of its own, comparing actual Broadridge invoices with transfer agent fee schedules for proxy processing services involving registered shareholders. Both of these studies demonstrate that issuers are overpaying for proxy services, when the current NYSE proxy fee schedule is applied, compared to free market pricing by transfer agents for proxy services to registered shareholders. As an example of the significant "profit" that broker-dealers are garnering from issuers, the latest STA cost study evaluated 20 actual Broadridge invoices and found that issuers would save an average of 42% over the NYSE fee schedule in a competitive market for proxy services.[18]

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[17] Id.

[18] The Securities Transfer Association, 2011 Transfer Agent Survey to Estimate the Costs of a Market-Based Proxy Distribution System, at 4-5, October 3, 2011, available at http://www.stai.org/pdfs/sta-survey-proxy-processing-costs-10-3-11.pdf; See also The Securities Transfer Association, Estimated Cost Savings of a Market Based Proxy Distribution Model, October 14, 2010, available at http://www.stai.org/pdfs/STA-White-Paper-10-14-2010.pdf.

The NYSE Rule Proposal Failed to Address Inappropriate Charges to Issuers for Separately Managed Accounts

For several years now, broker-dealers have been charging issuers a series of proxy fees for separately managed accounts at the beneficial owner level. These are accounts in which a shareholder has delegated investment discretion and proxy voting authority to an investment adviser. One form of separately managed account is called a "wrap fee account," and current SEC rule interpretations do not permit broker-dealers to charge issuers any proxy fees for these accounts at the beneficial owner level.[19]

Despite these SEC rule interpretations, broker-dealers and their service providers charge a basic processing fee, an intermediary unit fee, a paper and postage elimination fee, and a proxy voting fee for each beneficial owner participating in a separately managed account program.[20] These proxy fees are being charged despite the fact that investors in these accounts are not receiving—or expecting to receive—any proxy materials and are not casting any proxy votes.

These separately managed account charges can add up to more than $1.00 per beneficial owner position, and the STA has estimated that issuers are being overcharged more than $50 million each year as a result of this billing practice.

Both wrap fee accounts and separately managed accounts function in the same manner regarding proxy voting activities. In both cases, the sponsor of these investment programs receives one package of proxy materials on behalf of each issuer holding a shareholder meeting. Acting in its capacity as an investment adviser, this sponsor then casts proxy votes in lieu of the beneficial owners who have delegated proxy voting authority as a part of these investment programs.

The broker-dealers that sponsor these discretionary account programs are well-compensated for their services, primarily through asset-based fees applied to these individual accounts. The documentation and data processing for both wrap fee accounts and separately managed accounts are standardized within a broker-dealer's accounting platform. Both types of accounts are flagged at the time they are created for the broker-dealer's own purposes, as well as to suppress transaction confirmations and issuer communications at the beneficial owner level. For the purpose of proxy voting, these accounts as a group only require the distribution of one proxy package—either by mail or electronically—to each investment adviser possessing delegated voting authority.

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[19] See, e.g., Status of Investment Advisory Programs Under the Investment Company Act of 1940, SEC Release No. IC-22579, 62 Fed. Reg. 15,098, at 15,105 (Mar. 31, 1997) ("[I]f a client delegates voting rights to another person, the proxies, proxy materials, and, if applicable, annual reports, need be furnished only to the party exercising the delegated voting authority.").
[20] Broker-dealers also charge a Notice and Access fee for these beneficial owner positions when an issuer uses this format.

Any processing or programming functions necessary to segregate these accounts for proxy voting purposes should be taking place at the broker-dealer level and before any information is transmitted to Broadridge or any other service provider.[21] The issuer should not be responsible for any "preference management" involving these accounts, as it is only responsible for providing one proxy package to the sponsor of one of these investment programs.

In its report, the PFAC claimed that "a significant part of the work involved [for separately managed accounts] was in 'maintaining' or 'managing' the preferences attached to each account position."[22] This is despite testimony presented to the PFAC that almost all beneficial owners in managed accounts make a single election not to receive proxy materials and to delegate their voting rights to the investment manager at account inception—a simple account flag applied once an account is opened. Apart from an account flag being read by a computer program, the PFAC does not discuss in its report what additional efforts are required to justify the "significant work" of managing these account preferences.

Despite this lack of detailed analysis, the PFAC decided that fees for separately managed accounts should remain an issuer expense, as the maintenance of the investor "preference" should be handled in the same manner as in any other beneficial owner election, such as consenting to electronic delivery. The PFAC also stated that issuers benefit from the additional votes they receive from investment advisers, even though these advisers are required to vote as fiduciaries under SEC and Department of Labor rules.

In response to criticisms over charges for separately managed accounts, the PFAC did elect to exempt any shareholder position holding 5 shares or fewer in a managed account from all proxy fees. However, the STA estimates that the benefit of this proposed change would only be a reduction in managed account charges of 5.49%.[23]

To add insult to injury, the PFAC report also recommends that wrap fee accounts be *added back* to issuer invoices as billable positions and charged in the same manner as separately managed accounts, despite SEC interpretations that say otherwise.[24]

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[21] The STA understands that at least one large broker-dealer, Merrill Lynch, does not send Broadridge (or to other broker-dealer agents) any beneficial owner information for customers in its wrap fee account and separately managed account programs.
[22] NYSE PFAC Report at 13.
[23] See The Securities Transfer Association, Analysis of Proposed NYSE Proxy Fee Schedule, at 17, July 12, 2012, available at http://www.stai.org/pdfs/sta-analysis-of-nyse-pfac-proposed-proxy-fees-final-7-10-2012.pdf.
[24] See, supra, note 19.

The STA brought the separate managed account fee issue to the attention of the SEC more than two years ago, and it was highlighted in the SEC's Concept Release in July 2010.[25] In 2011, the STA filed separate written complaints with FINRA and NASDAQ about this issue, during the period the PFAC was conducting its evaluation of proxy fees.[26] Earlier this year, the STA and the Shareholder Services Association ("SSA") filed jointly a Petition for Rulemaking at the SEC, requesting that the agency prohibit broker-dealers and their agents from charging issuers any proxy fees for separately managed accounts.[27] To date, no action by either the SROs or the SEC has been taken in response to these complaints and requests.

Conclusion

The STA believes that proxy fees should be set at a level that reflects a reimbursement for reasonable expenses, as SEC rules require. More attention needs to be focused on what the true cost of providing these proxy services is, as the proxy fee schedule proposed by the NYSE will only lock in fees that are clearly financing activities that are not the responsibility of issuers.

The STA's own cost studies confirm that issuers are not paying for proxy services at the free market price of obtaining these services. In its 2011 examination of 20 Broadridge invoices, the STA found that using the fee schedules for its six largest transfer agent members would save issuers more than 42% in a competitive marketplace for proxy services.

The STA urges you to disapprove this NYSE proposed rule, as it does not meet the standards you have articulated for SRO rulemaking. As you noted in your Statement of May 14, 2012, regarding the SEC's approval of MSRB Rule G-17 Interpretive Notice:

> If there is any question as to the rigor of an SRO's analysis, then it is all the more paramount that the Commission not defer to the SRO's claims, conclusions, and judgments. The Commission has a

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[25] Letter from Thomas L. Montrone, The Securities Transfer Association, to Mary L. Schapiro, Chairman, Securities and Exchange Commission, June 2, 2010, available at http://www.stai.org/pdfs/STA_Letter_to_SEC_re_Managed_Accounts_6-2-2010.pdf; and SEC Concept Release at 42, 997.

[26] Letter from Charles Rossi, President, The Securities Transfer Association, to Richard G. Ketchum, Chairman and Chief Executive Officer, Financial Industry Regulatory Authority, October 31, 2011, available at http://www.stai.org/pdfs/2011-10-ketchum-letter.pdf; and Letter from Charles Rossi, President, The Securities Transfer Association, to Robert Greifeld, Chief Executive Officer and President, The NASDAQ OMX Group, November 9, 2011, available at http://www.stai.org/pdfs/2011-11-sta-letter-to-robert-greifeld-nasdaq.pdf.

[27] The Securities Transfer Association and the Shareholder Services Association, Petition for Immediate Regulatory Action Regarding Issuer Invoice Payments to Broker-Dealers for Separately Managed Accounts, SEC File No. 4-647, March 12, 2012, available at http://www.sec.gov/rules/petitions/2012/petn4-647.pdf.

> fundamental oversight role with respect to SROs, and undue deference to an SRO in the SRO rulemaking process undercuts the basic structure of that regulatory relationship.[28]

The process followed by the NYSE in developing this rule proposal was not a rigorous or independent process. In its place, the NYSE should be required to follow the recommendation of its 2006 Proxy Working Group and undertake an independent review of its proxy fee schedule, including an evaluation of the costs of providing proxy processing services and the contractual arrangements between broker-dealers and their service providers.

Thank you for your consideration of these views.

Sincerely,

Charles Rossi
President
The Securities Transfer Association, Inc.

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[28] Gallagher and Paredes Statement, supra, note 6.