



September 22, 2010

Elizabeth M. Murphy  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

Re: File No. S7-14-10; Concept Release on the U.S. Proxy System

Dear Ms. Murphy:

The American Business Conference (ABC) is a Washington-based coalition of midsize growth companies founded in 1981 by Arthur Levitt, Jr. The chairman of ABC is Alfred P. West, Jr., Chairman and CEO of SEI Investments, Oaks, Pennsylvania.

We are writing to offer comments on the Commission's concept release on the proxy system.

Over the years, ABC has submitted a number of comment letters to the Commission on aspects of the proxy system.<sup>1</sup> We have offered our views in presentations before the Proxy Working Group of the New York

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<sup>1</sup> See, e.g., Letter of John Endean to Jonathan G. Katz, Secretary, U.S. Securities and Exchange Commission, Re: File No. S7-19-03, Security Holder Director Nominations, March 31, 2004; Letter of John Endean to Jonathan G. Katz, Secretary, U.S. Securities and Exchange Commission, Re: Rule No. 4-493, Business Roundtable Petition for Rulemaking Regarding Shareholder Communications, July 19, 2004; Letter of John Endean to Nancy M. Morris, Secretary, U.S. Securities and Exchange Commission, Re: File No. S&-10-05, Internet Availability of Proxy Materials, February 16, 2006; Letter of John Endean to Nancy M. Morris, Secretary, U.S. Securities and Exchange Commission, Re: File Numbers S7-16-07 and S7-17-07, Shareholder Proposals and Shareholder Proposals Relating to the Election of Directors, October 5, 2007; Letter of John Endean to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, Re: File No. SR-NYSE-2006-92, Proposed Amendment to New York Stock Exchange Rule 452, March 31, 2009.

Stock Exchange and at a 2007 Commission Roundtable on proxy mechanics. We have also discussed proxy-related issues in the press.<sup>2</sup>

ABC has always tried to point out areas where we think the U.S. proxy system could be incrementally improved. At the same time, we believe, in the words of the chairman of the Commission-initiated Proxy Voting Review Committee, that the U.S. proxy system is the “finest proxy system in the world,” and that its “integrity, efficiency, fairness, audit ability [sic] and reliability...must be maintained,” especially, we would add, in the face of persistent but misguided efforts to reformulate the system beyond recognition.<sup>3</sup>

**Summary of Comments on the Concept Release** This comment letter touches on three issues raised in the concept release: client directed voting, proxy advisory firms, and proposals to make the so-called “street- side” proxy process resemble more closely the workings of the “registered side,” essentially by extracting brokers from the street side process. In summary:

- ABC believes that client directed voting (CDV) is the best tool available to meet the Commission’s desire to raise the abysmally low percentage of individual shareholders who vote in corporate elections.
- ABC regards proxy advisory firms as legitimate entities whose relationship to their shareholder clients requires more transparency. Their use by institutional investors has, in our

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<sup>2</sup> See, e.g., John Endean, “A Snipe Hunt,” *Directors & Boards*, First Quarter, 2007; Mary Beth Kissane, “Breaking the Broker Vote,” *Corporate Secretary*, July 2007, pp. 30 – 32; John Endean, “Endangered: The Individual Shareholder Vote,” *Directors & Boards E-Briefing*, <http://www.directorsandboards.com/DBEBRIEFING/DBeletterAPRIL09.html>, April 2009; Frank G. Zarb, Jr. and John Endean, “The Case for Client-Directed Voting,” *Law360*, <http://www.law360.com/articles/140395>, January 4, 2010; Frank G. Zarb, Jr. and John Endean, “Restoring Balance in Proxy Voting: The Case for Client Directed Voting,” *Harvard Law School Forum on Corporate Governance and Financial Regulation*, <http://blogs.law.harvard.edu/corpgov/2010/02/14/>, February 14, 2010.

<sup>3</sup> Remarks of Steven Norman, Executive Summary of the Proxy Voting Review Committee, Submitted to Ms. Sharon Lawson, Senior Special Counsel, Office of Market Supervision, SEC Division of Market Regulation by Richard H. Koppes, Facilitator & Secretary, PVRC, February 28, 2002, p. 11.

view, undermined the assumption that the criteria for voting decisions compliment and reinforce investment decisions, with shareholder value the bedrock goal of both.

- ABC opposes a massive overhaul of street side proxy mechanics because it would put at risk the current, reliable turn-key process with its proven track record of benefiting issuers and investors alike.

***Client Directed Voting*** In the ongoing and ever-expanding debate over corporate governance, large public companies are ably represented by groups such as the Business Roundtable (BRT). Institutional investors enjoy the benefits of membership in the Council of Institutional Investors (CII) while the big brokerage firms, corporate secretaries, and other interested parties have their own organizations.

There is no cognate group representing the interests of individual investors. That task necessarily falls to the Commission. Part of that task involves finding ways to encourage retail shareholders to vote their shares.

In various public statements, members of the Commission seem to accept this responsibility.<sup>4</sup> And yet, in recent years, we have seen the Commission act in ways that have, however inadvertently, suppressed the individual shareholder vote.

We have in mind here the so-called “notice and access” rules. These rules, in many ways excellent, have reduced voting by individual shareholders. Similarly, the Commission’s ritual disembowelment of the broker discretionary vote, despite the extremely promising

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<sup>4</sup> See, e.g., The Honorable Elisse B. Walter, “Restoring Investor Trust through Corporate Governance” – remarks before the Practising Law Institute, February 18, 2009, available at <http://www.sec.gov/news/speech/2009/spch021809ebw.htm>; and The Honorable Luis A. Aguilar, “Increasing Accountability and Transparency to Investors,” – remarks at The SEC Speaks in 2009, February 6, 2009, available at <http://www.sec.gov/news/speech/2009/spch020609laa.htm>.

“proportional voting” innovation, has been just as damaging for the communication of the views of individual shareholders.<sup>5</sup>

In this context, it is important for the Commission to push ahead immediately with client directed voting.<sup>6</sup> We believe CDV is a matter separate and separable from the other parts of this concept release and should be so treated. The Commission should initiate a pilot CDV program in cooperation with a brokerage firm with a sufficiently large sample of retail clients.

This is the only way we can think of to test CDV and to determine whether criticisms and concerns expressed by some informed observers have any validity.<sup>7</sup> It is also the only way we can think of for the Commission to demonstrate substance behind its rhetorical commitment to raise the level of individual shareholder participation in the proxy process.

***Proxy Advisory Firms*** When the federal government mandated that institutional investors vote their portfolio stock in every corporate election, it created an entrepreneurial opportunity that led to the rise of proxy advisory firms. This seems to us a perfectly natural turn of events.

The problem presented by proxy advisory firms is not their existence. It resides in their apparent lack of accountability to the beneficial owners of the securities managed by the firms’ institutional investor clients. This lack of accountability is rooted within the structure of the institutions. It has been best described by the attorney Charles M. Nathan of Latham & Watkins LLP.

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<sup>5</sup> Letter of John Endean to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, Re: File No. SR-NYSE-2006-92, Proposed Amendment to New York Stock Exchange Rule 452, March 31, 2009.

<sup>6</sup> We note the Commission staff’s curious decision, in the concept release, to call CDV “advance voting instructions.” In this letter, we do not use “advance voting instructions.” After all, under CDV a beneficial owner can change those instructions at any time – they are not set in concrete “in advance.” Moreover, for us, aware as we are of the skepticism of some regarding CDV, the “advance voting instructions” moniker carries an unfortunate hint of hospital directives such as “do not resuscitate.”

<sup>7</sup> See, e.g., Alan L. Beller, Janet L. Fisher and Rebecca M. Tabb, “Client Directed Voting: Selected Issues and Design Perspectives,” a White Paper commissioned by the Council of Institutional Investors, August 2010.

In an analysis that parallels Berle and Means's famous Depression-era critique of the modern corporation<sup>8</sup> – specifically, the separation of ownership and control – Nathan finds a “discontinuity at most institutional equity investors between the persons who make the buy and sell decisions...and those who make the decisions on how to vote portfolio shares.” The former seem entirely too preoccupied with wealth creation to be much bothered by voting while the latter live in an ideological echo chamber divorced from the basic economic interests of beneficial owners.<sup>9</sup> If the disconnected internal structure of institutional investors that Mr. Nathan describes is as widespread as he implies, many voting decisions made by institutions are uninformed by the shareholders' basic economic investment purpose.<sup>10</sup>

Proxy advisory firms have amplified, but did not create, this dilemma. Their business is to be the “cheaper provider of the application of one-size-fits-all voting policies to the tens of thousand of proxy votes needed each proxy season.”<sup>11</sup> In other words, they provide outsourcing services

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<sup>8</sup> Adolf A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property*, Revised Edition, (New York: Harcourt, Brace, and World, 1967). This study was first published in 1932.

<sup>9</sup> Charles M. Nathan, “The Future of Institutional Share Voting: Three Paradigms,” *The Harvard Law School Forum on Corporate Governance and Financial Regulation*, <http://blogs.law.harvard.edu/corpgov/2010/07/23/the-future-of-institutional-share-voting-three-paradigms/>, July 23, 2010. Those interested in the perverse results that this “circular process of validation of corporate governance ideas” can yield need look no further than the 2004 recommendation by Institutional Shareholder Services to its clients to withhold support for the reelection of Warren Buffett to the board of Coca Cola. Alice Schroeder, *The Snowball*, (New York: Bantam Books, 2008), pp. 778 – 781.

<sup>10</sup> Some commentators minimize the discontinuity between the fiduciary interests of beneficial owners and the recommendations of proxy advisory firms. See, e.g., Stephen Choi, Jill Fisch, and Marcel Kahan, “The Power of Proxy Advisors: Myth or Reality?” *Emory Law Journal*, Vol. 59, 2010, PP. 869 – 918. While the authors find much about proxy advisory groups “troubling,” they add, “We found a substantial correlation between proxy advisory recommendations and the factors that academics, policy makers, and the media have identified as important. This correlation challenges the view that...proxy advisors are causally significant in determining the shareholder vote because shareholders may themselves directly consider these factors important.” ABC's alternative interpretation of this phenomenon is that it is another illustration of the “circular process of validation of corporate governance ideas” amongst elites, which, again, may be unrelated to the economic interests of beneficial owners.

<sup>11</sup> Nathan, *op.cit.*

and in so doing they abet the “discontinuity” between institutional investment and proxy voting.

That the proxy advisory firms are so well entrenched in the voting process may create an opportunity for the Commission to address this discontinuity of investment and voting decisions within large shareholders.

While the Commission apparently lacks the authority to require a pension fund or other institutional investor to connect its “economic” side with its voting side, it can require greater transparency regarding the way they use proxy advisory firms in the voting process. Just as disclosure makes corporate boards more accountable to shareholders, greater disclosure from proxy advisers should help ensure that their large institutional investor clients use their voting power in a way that is consistent with their economic fiduciary obligations.

Specifically, the Commission should require all proxy advisory firms to register as investment advisers. It should then require proxy advisers who vote shares on behalf of institutional clients to disclose the name, position, and responsibilities of the client representative who directed the proxy adviser to vote shares, as well as the nature of the direction given.

As an additional step, the proxy advisory firm should provide the Commission with a client certification that the person who makes investment decisions for the client fund has been furnished all relevant proxy materials, has reviewed the voting decisions, and approves the vote or votes as consistent with the fiduciary duty of the fund to vote its shares in the interest of its beneficiaries.

Proxy advisory firms play a crucial facilitating role in decisions about proxy voting by large, economically important institutional funds. ABC believes that some modest changes in favor of greater disclosure and certification could go a long way to building confidence in the way such firms do business.

**Reform of the Beneficial Shareholder Proxy Process** While ABC is always open to innovation in regard to the proxy process, we are skeptical of proposals for wholesale change. In our view, the beneficial shareholder (street-side) proxy process works exceedingly well and we are not aware of any fully-articulated alternative that gives us confidence of improvement over the *status quo*.

Critics of the street-side process tend to gloss over, or, worse, denigrate, its central achievement: corporate elections conducted and tallied by an independently audited central processor that yields accurate and timely results without a hint of conflict-of-interest or accusations of fraud. It constantly amazes us that this fact is so little celebrated, although it is central to the maintenance of public confidence in our economic system. It is no small achievement, and as more and more controversial issues find their way onto proxy ballots, it is one that ought to be especially valued by the Commission.

Moreover, according to available data, the street-side system has delivered significant overall cost savings to issuers of all sizes. As far as we can discern, proxy fees have remained steady in nominal terms over the past eight years, which means, in real terms, a 17.5 percent decline.<sup>12</sup> In addition, the overall cost of the proxy process has been reduced through automation and through the elimination of waste in printing and mailing.

The cost efficiencies of the street-side proxy process are far superior to those incurred on the registered side. According to a study by the economic consulting firm Compass Lexecon, the cost of proxy processing for registered shareholders was on average 36 percent to 40 percent higher than for street-name holders. For the very smallest public companies, the cost of registered processing is more than double the cost for street-name holders.<sup>13</sup>

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<sup>12</sup> Compass Lexecon, "An Analysis of Beneficial Proxy Delivery Services," May 11, 2010, p. 11. Compass Lexecon is an economic consulting firm. This study was undertaken with the sponsorship of Broadridge Financial Solutions, Inc.

<sup>13</sup> *Ibid.*, pp. 27 – 29. According to Compass Lexecon, Broadridge also functions as a transfer agent on the registered side. The price comparisons in the Compass Lexecon study use registered side data from Broadridge since information from other transfer agents was not available. The comparisons are consistent with informal reports from ABC members. If other transfer agents wish to produce their own pricing data, ABC would be happy to see it.

Despite these facts, over the last fifteen years, the beneficial shareholder proxy process has endured considerable scrutiny both in terms of its operation and its fee structure. Emphasis on the street-side was inevitable given the declining role of registered shareholders.

The current concept release is yet the latest example of this scrutiny. In part, it has its roots in a 2004 petition for rulemaking filed with the Commission by the Business Roundtable (BRT) and supported by Georgeson, a proxy solicitation firm and by the American Society of Corporate Secretaries. This petition for rulemaking called upon the Commission to “conduct a thorough review of the current shareholder communications system,” with a focus on the street-side.<sup>14</sup>

A few years later a group calling itself the Shareholder Communications Coalition (SCC) and consisting of the BRT, the Securities Transfer Association (STA) and other associations, renewed the BRT’s original demand for a review of the street side process. It has also proffered a bouquet of ideas that it calls a “Proxy Process Reform Plan.”<sup>15</sup>

As we understand it, SCC wants to remove brokers from the proxy process and eliminate Broadridge Financial’s role as the central proxy processor. The result would be a decentralized system, very much like the current registered side, that would leave companies to manage not only the substantive and procedural details of their annual meetings but the voting process as well. This latter function would almost certainly be outsourced to a firm that specialized in that service – Broadridge, of course, and also various transfer agents whose business on the registered side has been drying up as the number of registered shareholders has dwindled.

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<sup>14</sup> Letter of John Endean to Jonathan G. Katz, Secretary, U.S. Securities and Exchange Commission, Re: Rule No. 4-493, Business Roundtable Petition for Rulemaking Regarding Shareholder Communications, July 19, 2004

<sup>15</sup> Other members of SCC are the National Investor Relations Institute and the Society of Corporate Secretaries & Governance Professionals (formerly the American Society of Corporate Secretaries). Although SCC’s website also names the National Association of Corporate Directors as a member, we believe NACD is no longer a part of the group. See <http://www.shareholdercoalition.com/about.html>. The SCC’s ideas are contained in a letter with attachment from its executive director, Niels Holch to the Honorable Mary L. Schapiro, Chairman, U.S. Securities and Exchange Commission, August 4, 2009.

The last thing ABC would like to see is the street-side proxy process “reformed” to function like the more expensive, less efficient registered side with all the inevitable charges of voter fraud that would accompany such a change if companies managed their own shareholder votes. We have no desire to erect yet another Disneyland for lawyers.

That said, we can certainly understand why large companies and transfer agents, and perhaps Broadridge as well, would find the change more appetizing. Transfer agents, without changing their business model, would finally have a shot at gaining market share on the street-side. As for large companies, they would be able to shed the fixed proxy fee system – which, in fact, benefits them at the expense of smaller firms – and use their size to extract even better deals from the largest and most efficient voting service providers.

Of course, smaller public companies would have no such leverage. They would be at the mercy of the big brand name service providers such as Broadridge and Computershare, who will dictate terms on a take-it-or-leave-it basis. This cream-skimming scenario is eerily reminiscent of what happened to the bidding for accounting services after the demise of Arthur Andersen and the passage of Sarbanes-Oxley legislation.

ABC members are sometimes told that the SCC “reform” proposal would enable them to communicate more freely with their shareholders and, in fact, to know who those shareholders are. ABC members have never reported frustration in communicating with their retail shareholders and we doubt that this is a top-of-the-mind matter for most companies. The debate over ending the OBO/NOBO distinction, in short, has little immediate relevance. The big issue for our companies is their need for timely information about the identity and intentions of large shareholders. Activist hedge funds have raised the specter of shareholders building large positions quickly and avoiding required reports through a variety of means. We do not see this problem as a proxy process matter. Instead, what is important to ABC members is improving the timeliness or perhaps lowering the thresholds for large position reporting under the Williams Act. ABC thus prefers an emphasis on affirmative disclosure requirements over the promise of easier access to ever-changing shareholder lists.

We would make one final point and that is about the desirability of competition in the street-side proxy process. The concept release asks: “Is competition in the proxy distribution service needed, and if so, what changes to facilitate issuers’ communications with investors would also encourage competition in the proxy distribution service?”

Certainly, if we had our choice, Broadridge would be faced with significant competition from other companies. ABC believes in competition.

However, we do not favor upending the entire street-side process, with all the uncertainty and inequities that entails, for the mere sake of attempting to create that competition. Over the years of working on proxy issues, we have heard Broadridge talked about in terms reminiscent of the way people talked at various times about General Motors or IBM, or Microsoft – companies supposedly with unassailable competitive positions invulnerable to competition, absent positive government action. We do not find this analysis any more convincing regarding Broadridge than we did in regard to those earlier, once-dominant firms.

This is not the place for market analysis, but it is worth pointing out that the street-side presents a growing market opportunity, if only because the number of shareholders is increasing. Nor does it seem that Broadridge has a lock on that opportunity. According to information made public by the Council for Institutional Investors, Broadridge’s contracts with brokers or bank custodians “average three years in length [with] one-third...up for renewal and re-bid each year.”<sup>16</sup> There are apparently three firms that currently compete with Broadridge for this business.<sup>17</sup>

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<sup>16</sup> Broadridge’s August 2009 Responses to CII Subcommittee’s Proxy Voting Questions, p. 4. available at: <http://www.cii.org/UserFiles/file/members%20login/ProxyVotingSubcommittee/Proxy%20Voting%20Questions%20-%20Broadridge%20Responses%20August%202009.pdf>

<sup>17</sup>Securities Industry and Financial Markets Association, “Report on the Shareholder Communications Process with Street Name Holders, and the NOBO-OBO Mechanism,” June 10, 2010, note 13, P. 24. The three competitors of Broadridge are Mediant Communications, ProxyTrust, and INVEeSHARE.

There will be even more competition for Broadridge as potential competitors develop new and better ideas or technologies to service the street-side. In the meantime, ABC, with respect, does not believe that the Commission ought to spend a moment more of its increasingly valuable time contemplating regulatory changes to affect the competitive marketplace, particularly if such changes would put at risk the efficiencies and integrity of the street-side proxy system, which has worked so well for issuers and investors alike.

We thank the Commission for its attention.

Sincerely,

A handwritten signature in cursive script that reads "John Endean". The signature is written in dark ink and is positioned above the printed name and title.

John Endean  
President