Securities Regulation Daily Wrap Up, PROXIES—Proxy voting mechanics and technology examined at SEC roundtable, (Nov. 19, 2018)

Securities Regulation Daily Wrap Up

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In the first of three panel discussions on the U.S. proxy process, representatives from industry and investor groups shared ideas on how to improve the accuracy, transparency, and efficiency of the proxy voting and solicitation system and how technological advances might be used to enhance the voting process. The SEC hosted the proxy roundtable, which also featured discussions on improving shareholder engagement and the role of proxy advisory firms.

Corporation Finance Director William Hinman welcomed the panelists, advising that private market solutions can be faster, more flexible, and less intrusive than regulatory solutions, so the SEC benefits greatly from industry feedback. He also drew attention to a concept release published by the Commission on the proxy process in 2010, noting that many of the issues raised in the concept release still exist today.

Advisory committee input. Professor John Coates of Harvard Law School acknowledged that of the three topics to be discussed by the roundtable, this topic was the "most boring," but he also said that it was the least partisan and the most important. He outlined some of the main themes gleaned from a recent meeting of the Commission's Investor Advisory Committee (IAC), which had discussed the proxy process at length. There is a general concern that retail participation in proxies is down, even in contested elections where voting can play a pivotal role, he said. One reason for this is the OBO/NOBO system that creates differences in communications with retail investors. Non-objecting beneficial owners (NOBOs) allow intermediaries to release their names and addresses to the issuer, while OBOs are shareholders who do not allow their identities to be disclosed. Coates suggested that the SEC conduct a survey to determine why some shareholders do not choose to be NOBOs and then think about how the industry can respond.

Members of the IAC had also emphasized that shareholders want to know that their votes were actually counted, Coates said. He noted that there are solutions that currently exist, and urged Broadridge Financial Solutions, which provides proxy voting services, to think how it can make its system simpler. In addition, the IAC observed that the many layers of intermediation can produce mismatches in information, which can lead to the disqualification of votes, Coates said.

Systemic change needed, but short-term fixes are available. Nudges from regulators alone will not be sufficient to improve the system, according to Ken Bertsch, executive director of the Council of Institutional Investors. In CII's view, it is time for a fundamental rethink of the proxy voting system. In terms of regulation versus market forces, the SEC should lead the thought process to find out what makes sense, Bertsch said. While the technology is available that can be used in this area, a fundamental change will take time, and the Commission should look at short-term fixes.

In the near-term, the SEC should, through rulemaking or guidance, require all intermediaries to take steps to transmit all the necessary information to provide routine and reliable vote confirmation, Bertsch advised. The Commission should also issue guidance that leads to pre-reconciliation of discrepancies between broker-dealer and DTC positions to minimize differences.

OBO/NOBO issues. Katie Sevcik, executive vice president and COO of transfer agent EQ, suggested that many shareholders who are currently OBOs actually would prefer to be NOBOs. Even issuers that do have access to shareholders who are NOBOs find it expensive to gain access to the shareholder list, noting that one issuer

recently paid $70 per name. She also observed that NOBO lists do not use email addresses, meaning issuers can only reach out to these shareholders via postal mail.

Lawrence Conover, vice president at Fidelity Investments, pointed out that the largest percentage of OBOs are institutional investors. For them, it is a privacy issue, he said, and they will do anything to protect their privacy. Comparatively, most retail investors are NOBOs, he added.

Blockchain. Several roundtable participants expressed support for using blockchain or other distributed ledger technology to reform the proxy voting system. Robert Schifellite, president of investor communications at Broadridge, said that his company is making very significant investments in blockchain, including a pilot program with Bank Santander as well as blockchain pilots in the U.S. with five issuers and a couple of custodians. He highlighted Broadridge's platform and invited those interested to come see how it works, the controls that have been implemented, and audits that take place to ensure that the process is accurate and reliable.

Alexander Lebow of A Say Inc. was more cautious to embrace blockchain, although he acknowledged that the technology holds great promise with regards to proxies. According to Lebow, there is a spectrum of approaches to blockchain, with one end being the complete reconstruction of the equity markets with distributed ledger technology and the other end involving certain layers of blockchain on top of a pre-existing system. In his view, the more you move away from an all-in reconstruction of the system towards "layers of veneer," the fewer the benefits will be and the less clear the advantages are over existing database technologies. "If you're going to do it, you need to go all-in on blockchain," he advised.

Chairman Jay Clayton praised the roundtable's participants and said he was heartened to hear about technology and stressed that the technology should not drive the structure; rather, we should outline our goals and then find the technology that can help address these goals.

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