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Questions surround proxy firm that botched Yahoo vote count

Broadridge called into question after miscue in Yahoo vote; 'a lot of times these problems aren't caught'

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An embarrassing vote-counting error revealed after Yahoo's high-profile annual shareholder meeting this month has renewed concerns about the way investor votes are tabulated in the U.S.—and raised questions about the company with a near-monopoly on the business of processing shareholder votes: Broadridge Financial Solutions.

A printing error led most Yahoo shareholders to believe that embattled CEO Jerry Yang had received the support of 85% of shareholders, when in fact a recount revealed only 66% supported him. After Broadridge was notified of the glitch, it fixed it within minutes, the company says, but news of the slipup raised more than a few eyebrows. Indeed, if a large hedge fund hadn't made a stink after the 85% figure was released, the error might not have been noticed at all.

Some have noticed, though. "We believe the system needs to be carefully inspected to determine what other errors could occur and increase transparency," the Florida State Board of Administrators, which runs the state pension fund, said in a statement to Financial Week. "We hope the Yahoo voting error was an anomaly, but without further ability to confirm the votes cast, investors and companies are left without recourse."

Chuck Callan, senior vice president of regulatory affairs at Broadridge, said the mistake reflected a confluence of unusual factors, including a large shareholder submitting a huge number of dissenting votes for a single nominee. As a result, the eight digits typically allotted for tallies of dissenting shareholder votes were not enough to catch the total votes cast against Mr. Yang.

No similar errors have occurred in the last five years at Broadridge, Mr. Callan insisted, adding that the Lake Success, N.Y., company has taken steps to ensure similar snafus are avoided.

Nevertheless, several corporate governance and investor relations experts say they've been burned by Broadridge in the past.

"What we have now doesn't work," observed Meagan Thompson-Mann, a visiting research fellow at Yale University's Millstein Center for Corporate Governance, who authored a paper in June criticizing the company and calling for a public commission on proxy modernization. "You sit at a desk, you press a button, and you put a lot of faith in Broadridge. [But] a lot of times these problems aren't caught."

When she served as corporate governance counsel at the Railways Pension Trustee from 2003 to 2007, Ms. Thompson-Mann said, Broadridge mistakenly stated the U.K. fund could vote shares on loan to other parties, even though regulations there forbade it.

Other critics, including New York University professor Marcel Kahan and University of Pennsylvania professor Edward Rock, say Broadridge has too much power in the U.S. In an August 2007 paper, the duo said Broadridge is "an accident waiting to happen" and suggested it be removed "from its position as the key, monopolistic actor at the center of the spiderweb," noting the firm has "a very profitable business" and would likely "oppose any substantial reform."

Big investors seem to have complaints too. At a February voting standards roundtable convened by the Millstein Center and attended by institutional investors, several participants reportedly complained that Broadridge did not have a good way of verifying how votes are cast.

The Council of Institutional Investors declined to comment for this story, as did the California Public Employees' Retirement System, the largest institutional investor in the country, both of which sent representatives to the event. But a Florida pension official described how Broadridge had mistakenly split the votes from that state's fund, even though the fund always voted its shares unanimously, alleging that Broadridge was unable to verify the votes and explain how the problem occurred.

Broadridge declined to respond to what it called "anecdotes." Mr. Callan said a steering committee that includes institutional investors and corporate issuers regularly audits the company's processes and regulatory compliance. The Securities and Exchange Commission and the New York Stock Exchange also meet with the company about once a year to discuss issues and examine some of its processes.

According to Broadridge, a survey completed in June found nearly all of a random sample of some 6% of its institutional investor clients rated its service good, very good or excellent. An NYSE working group two years ago also stated that ADP (Broadridge's predecessor company, which spun off Broadridge last year as its own public company) was "viewed by the institutional community as impartial, reliable and efficiently administered."

Over the last two decades, banks and brokers have outsourced proxy services, and Broadridge has become the dominant company in the areas of sending voting instructions, executing proxies on behalf of banks and brokers, and aggregating votes. Mr. Callan said the company provides vote tabulation services for only 1,000 of its roughly 8,000 clients, though it has been considering offering more tabulation services.

"We don't know of anybody else in this industry that has that level of transparency," he said, "or, frankly, that commitment to continuing to address the real

needs of participants in this marketplace."

If Broadridge is unrivaled in some of the safeguards it employs, that may be because it's unrivaled in its business model. The company is thought to act as the proxy agent for as many as 97% of banks and brokers in the U.S., which gives it a near-monopoly when it comes to tallying proxy votes here. (In Europe and elsewhere, the firm has true competitors.) According to its most recent 10-K filing, in 2008 Broadridge had net revenue of \$2.2 billion and a pretax profit margin of 14.8%.

Further, while Broadridge is regulated in some aspects of its business, such as its adherence to the new e-proxy notice and access rules, others seem to get overlooked.

"They are a critical component of the voting process, and nobody is watching them," said J. Robert Brown, a corporate governance and business law professor at the University of Denver. While the company may not be the official vote-counter in all cases, it still collects votes and should be able to tell investors how they voted, he said. "Broadridge has a big role in the tabulation process, even if it isn't always the tabulator."

Still, many experts say few transfer agents and brokers that verify votes for investors do much better than Broadridge, and note that the proxy voting system itself is broken, riddled with loopholes that allow over- and undervoting.

"Broadridge has done a lot to clear away obstacles, but it's a system that's jerry-rigged," said Stephen Davis, director of the Millstein Center and principal at Davis Global Advisors. "There are problems that are built into the system.... [And] outside the United States, the inaccuracies and failures are much greater."

With the rise of activist investors and more votes being made public—the mutual fund industry in recent years has been required to disclose many votes, and other institutional investors often do as well—the vote-counting system has clearly improved but has not yet evolved, said Pat McGurn, special counsel for RiskMetrics, a proxy advisory firm that competes with Broadridge in Europe but uses the company in the U.S.

The initial undervote at Yahoo was probably an isolated incident, but instances of votes cast but not recorded are not rare, Mr. McGurn said. "There's plenty of room for slippage."

He suggests the SEC or another regulator should step in to oversee how proxies are voted. However, many industry experts say the SEC has tied the issues of broker voting, over-voting and other quirks to the larger—and more contentious—issue of shareholder access to proxies.

Other recent developments highlight the growing complexity of proxy fights. The 2nd Circuit Court of Appeals is scheduled to hear oral arguments today on whether 6.4% of the votes cast by two hedge funds at railroad company CSX should be discounted because of disclosure violations. Depending on the court's decision, two directors who were elected to CSX's board could be removed.

Broadridge's role in the case? It processed some investor votes, but was not the official counter. Good thing, perhaps. The last thing this company needs these days is another controversy.

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