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A PROXY MODEL FROM OFFSHORE: U.S. PROXY SYSTEM LAGS IN TRANSPARENCY AND ACCURACY

Prepared By T. L. Montrone

Despite the recent meltdown in the financial sector, the securities settlement and clearing system in the United States arguably remains one of the most modern, sophisticated and well-regulated systems in the world. It is surprising, then, when one considers that the distribution of shareholder voting rights to beneficial shareholders is a 30+ year-old opaque process lacking in audits. The process is inefficient, antiquated, contains layered unnecessary expenses and inhibits communication between companies and their shareholders. The process in place today in America was established by arcane SEC regulations issued more than three decades ago. The results are what one would expect of a dated process - it is costly, ignores advances in technology and encumbers communications between companies and their shareholders. The lack of audited voting rights and recognition of all shareholders also disenfranchises beneficial shareholders.

It would appear that regulators don't need to look far to find a solution. There are proven shareholder disclosure models already in existence - and one doesn't even need a translator to discuss them - well almost. The voting distribution systems in many other countries including the United Kingdom, Australia, New Zealand and Hong Kong are far more in touch with today's requirements for transparency, accuracy and cost-effective, open shareholder communications. During a recent meeting held at the Society of Corporate Secretaries & Governance Professionals, a presentation on beneficial shareholder communication requirements and practical applications in these countries was provided by David Geddes, CEO of Orient Capital and John McMurtrie, Managing Director of the Link Group. The presentation revealed a shareholder ownership discovery and communications process that really serves both beneficial holders and issuers.

Under powerful legislative disclosure provisions, issuers in certain jurisdictions are able, through their service agents, to obtain from any shareholder, in any location (be they street name, custodians, banks or nominees) who is not the beneficial holder of its securities, disclosure of full details of the underlying beneficial owners of its shares. Such entities are obligated to transmit the shareholder names, addresses

and share positions within a prescribed time period ranging, depending upon each country's regulations, from as little as two business days to two weeks. There are no confusing NOBO and OBO regulations or other barriers to obfuscate the ownership positions. All of this though is on the premise that each issuer, through its transfer agent, maintains and has full access to, its share register. Issuers may then make use of disclosure legislation as frequently as they want: many issuers in the UK and Australia analyze their share registers to identify their real institutional and retail shareholders on a monthly, or even more frequent basis. The intelligence on ownership and ownership trends that this delivers is extremely powerful - not only does it underpin corporate actions, but it facilitates timely communication between the owners of the company and its management.

Fair Voting Rights

The obvious benefit of these disclosure processes is to correct the many ills of the current beneficial holder proxy system in the United States. The most egregious problem is disenfranchisement that occurs today in the U.S. due to stock lending and the over distribution of voting rights. Our system permits large-scale distribution of excess voting rights and the process is unable to be audited. Beneficial holders are masked behind a confusing veil of NOBO versus OBO status and cannot ascertain their own voting status with the company in which they own stock.

The system used in the United Kingdom and other countries transfers voting rights directly to the beneficial shareholders. This essentially places beneficial and registered shareholders on the same footing and with equal voting rights. Just as important, the files are balanced and voting rights are only distributed commensurate with the number of shares outstanding. Voting rights still travel with shares that are on stock loan, but the account lending the shares no longer has the voting right and is not transmitted to the issuer.

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Notice and Access, the First Full Year

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3. Know the Shareholders - If they're insider-controlled, and the insiders vote, it's a Notice-friendly world for them. For the majority who are institutionally-held, they will still want to consider what's on the slate.
4. To Solicit or Not Solicit - Do you work with a solicitor, who can help bring back the votes. Again, if there are concerns with full-blown Notice, you can always recommend adopting Hybrid delivery.
5. It's All in the Packaging - If the annual report is a serious marketing tool, it doesn't preclude adopting Notice-Only delivery; just be prepared by printing a larger stand-by quantity. Print even more if you traditionally include a coupon with your package.

The Notice must also include:

1. The date, time and location of the meeting;
2. A clear and impartial identification of each matter intended to be acted upon and the issuer's recommendation, without supporting statements, regarding those matters;
3. A list of materials available at the web site which must include the proxy card, proxy statement and annual report;
4. A means to communicate requests for paper or e-mail copies including:
 - a. A toll-free telephone number;
 - b. An e-mail address; and,
 - c. An Internet Web site address.
5. The shareholder control number required to vote on-line and instructions on how to access and vote on-line [but not by telephone!];
6. Information on how to attend the meeting and vote in person;
7. Provide a date by which the shareholder should request a copy to ensure timely delivery for execution and return of a proxy;
8. An Internet Web site address specific enough to lead shareholders directly to the proxy materials. The Web site address cannot be to a home page, the SEC EDGAR address or to some other section of a web site other than where the proxy materials are hosted. ■

A PROXY MODEL FROM OFFSHORE: U.S. Proxy System Lags in Transparency and Accuracy

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Shareholder Communications: Benefits Beyond the Proxy System

The advantages of this system extend far beyond the distribution of voting rights. Mr. Geddes pointed out that companies are accustomed to having live access to their full registered shareholders, as well as monthly updates of their beneficial owners. This not only enables these companies to track ownership trends and changes, but to strategically manage their registers, as well as their investor relations. The detailed understanding that they have of their shareholders on an ongoing basis gives them the ability to communicate frequently and directly with major investors and to develop an understanding of institutional investors' concerns and views. This transparency is an open record for all to view, but the format and access to the information doesn't provide an adequate mechanism for investment houses to poach investment strategies or customers from competitors.

This process also affords issuers with the ability to distribute rights to their current shareholders when issuers want to raise capital. The direct communication provided under this system increases the abilities of issuers to reach out to their shareholders for all types of communications. Delays and exogenous expenses have been weeded out of the system, providing a process that really serves the investment community as much as issuers and retail shareholders.

This system wasn't built overnight. However, industry experts have often expressed a belief that relatively minor changes in SEC regulations would quickly engender changes to the distribution systems here. The technological infrastructure is already largely in place between brokers, DTC and transfer agents. The current U.S. system certainly has supporters, but one doesn't have to look hard to see that these supporters have a self-serving economic interest. While the SEC has gone to great lengths to encourage Notice and Access to reduce wasted expenses and help the environment, the current system of layered, non-competitive expenses has served to thwart these gains for many companies. It is time for a change, and these examples of a working system illustrate that the benefits of change are far reaching. ■

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is a publication of The Securities Transfer Association, Inc. All STA Newsletter correspondence should be addressed to the Editor: Cynthia Jones, The Securities Transfer Association, Inc. at cjones@stai.org. Questions or comments on the Newsletter may also be directed to Cynthia Jones. For information about the STA, contact Carol Gaffney, The Securities Transfer Association, Inc., P.O. Box 5220, Hazlet, NJ 07730 or call (732) 888-6040 or fax (732) 888-2121.

Editor: Cynthia Jones, The Securities Transfer Association, Inc.

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