



**STATE BOARD OF ADMINISTRATION
OF FLORIDA**

**1801 HERMITAGE BOULEVARD
TALLAHASSEE, FLORIDA 32308
(850) 488-4406**

**POST OFFICE BOX 13300
32317-3300**

**CHARLIE CRIST
GOVERNOR
AS CHAIRMAN**
**ALEX SINK
CHIEF FINANCIAL OFFICER
AS TREASURER**
**BILL McCOLLUM
ATTORNEY GENERAL
AS SECRETARY**
**ASH WILLIAMS
EXECUTIVE DIRECTOR & CIO**

October 20, 2010

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission (SEC)
100 F Street, NE
Washington, DC 20549-0609

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

Dear Secretary Murphy:

The State Board of Administration (SBA) of Florida welcomes the opportunity to provide comments on the Concept Release on the U.S. Proxy System. The SBA manages the assets of the Florida Retirement System (FRS), the fourth largest public pension plan in the United States with 1.1 million beneficiaries and retirees. SBA assets under management, including the FRS and other client mandates, total approximately \$140 billion. The SBA's governance philosophy encourages companies to adhere to responsible, transparent practices that correspond with increasing shareowner value.

We are pleased with the commission's decision to publish a concept release on proxy reform. Proxy voting is the primary tool for shareowners to exercise their rights and enforce governance standards and accountability. With over 500 billion shares being voted every year at over 13,000 shareowner meetings globally, the SBA believes that there has been a growing need to address developing issues within the voting system in order to promote greater efficiency, transparent procedures, and enhance the accuracy and integrity of shareowners' votes. Recent events have called into question the accuracy of the system, which may distort the potential outcome of important votes, affect share value, and disenfranchise investors. We provide detailed commentary, listed by major topic area below, in no particular order of importance.

Role of Proxy Advisory Firms

Proxy advisory firms play an important role in helping pension fund managers fulfill their fiduciary duties with respect to proxy voting by providing an analysis of issues on the ballot, executing votes and maintaining voting records. Without proxy advisors and the services they offer to clients, the SBA would find it difficult to analyze and vote the volume of proxies demanded through our extensive global equity holdings. The global integration of the financial markets and the rise of complex multinational corporations have exacerbated the types and volume of proxy issues before shareowners. As a result, the role of independent proxy advisory firms is critical to assist investors in decoding voting items and providing valuable advice to shareowners. It is reasonable to expect proxy advisory firms to provide clients with substantive rationales for vote recommendations; minimize conflicts of interest and disclose the details of such conflicts; and correct material errors promptly and notify affected clients as soon as practicable.

The SBA actively uses the recommendations of proxy advisory firms to assist in making voting decisions. As a client, we routinely critique the proxy recommendations, research models, analytical framework, and governance policies of each of our external proxy advisory firms. We believe that such client feedback is vital to maintaining relevant

and accurate proxy recommendations. We feel that the proxy advisory firms should provide relevant research which supports their recommendations and disclose, to an extent, the methods upon which they make their recommendations. Proxy advisory firms are one of the few significant participants in the voting process that are not generally required to be registered or regulated by the Commission. SBA staff believes there should be additional transparency surrounding the application of policies and varied analytical methodologies used by proxy advisory firms and supports additional regulation of the industry, including requiring all proxy advisory firms to register with the Commission as investment advisors. The Commission should reexamine the applicability of Rule 14a-2(b)(3) to proxy advisory firms and related solicitation activity exemption.

Because of the possibility for conflicts of interest to arise for proxy advisory firms who consult companies on some of the same issues for which they provide shareowner recommendations, SBA staff supports proxy advisory firms being subject to regular audits in order to provide assurance that there are strong internal controls within the advisory firms, which prevent conflicts of interest from occurring. Independent external audits of proxy advisory firms' models and advice would also serve to ensure to clients the soundness and proper application of stated analyses and policies. Although the SBA's own experience with the quality and accuracy of proxy advice has been very good, there may need to be more examination of the frequency (and materiality) of research errors to ensure investors can rely on proxy advisory firms' recommendations. SBA staff support the disclosure by proxy advisory firms of their methodologies, guidelines, assumptions and rationales used in making their voting recommendations, as long as no proprietary methods or sources are released. External auditing of proxy advisory firms may provide greater discipline in the way vote recommendations are determined, thereby ensuring a better proxy voting system.

Although we do not believe that proxy advisory firms have undue control or are overly powerful in their role as advisors, for many institutional investors they are a major source of information with which proxy voting decisions are made. Some issuers and other market participants contend that proxy advisory firms have too much influence. Our own experience, combined with relevant market-wide voting patterns, strongly contradicts this assertion. For example, data on director elections clearly illustrates proxy advisory firms' limited influence. Of 15,044 baseline client recommendations for director nominees in 2010 by Institutional Shareholder Services (ISS), 13 percent were "withhold" or "against." The actual statistic for SBA proxy voting, for the same time period, stock universe, and director ballot item, was 25.1 percent ("withhold" or "against" votes). Of the 1,879 nominees receiving "withhold" or "against" baseline recommendations with available voting results, less than 5 percent failed to receive majority support from shareowners. The average shareowner support for nominees with a "withhold" or "against" baseline recommendation from ISS was 77 percent.¹

We have also measured the correlation of the SBA's actual voting decisions with several of the major proxy advisory firms. We've found the relationship between our actual votes and the firms' recommended votes to vary greatly, not only among different proxy advisory firms but also across different types of voting issues and time periods. SBA staff believes that proxy advisors' clout has been greatly exaggerated by many organizations which are divorced from the actual procedures used by institutional investors to make voting decisions. Such pundits may not have an adequate understanding of the investment decision making process and organizational context of large institutional investors. Investors' use of proxy advisors' services, whether governance research or vote execution, does not equate to the "outsourcing" of voting decisions. It is critical to recognize that proxy advisors' clients retain the ability to vote however they choose and in accordance with their own written voting guidelines. The SBA independently develops its corporate governance principles and proxy voting guidelines, but does rely heavily on the external research and synthesis of issuer filings performed by proxy advisory firms, in order to supplement the evaluation of ballot items. In sum, investors are ultimately accountable for proxy voting decisions cast in their own name and on behalf of their beneficiaries.

¹ Institutional Shareholder Services (ISS) Voting Analytics for Russell 3,000 annual meetings between January 1, 2010 and September 15, 2010.

As noted by the Council of Institutional Investors (CII), nine of the Council's 10 largest member funds do not currently delegate their voting decisions to a proxy advisor. These nine pension funds currently use their own proxy voting guidelines, which are updated continually or on an annual basis, to govern their voting decisions. SBA staff believes the internal approach to making voting decisions is similar among the overwhelming majority of registered investment advisors and other institutional investment organizations.

SBA staff fully supports the proposal for expanded investor disclosure of the proxy advisory firm(s) it has utilized in its proxy voting decisions, the extent to which the fiduciary has voted in accordance with the recommendations of proxy advisory firm(s), and the procedures employed by the investment fiduciary to make voting decisions.²

Over-Voting and Under-Voting

Another issue raised in the concept release was the over- and under-voting of shares. This issue arises because of the overly-complex network of intermediaries in the share ownership system. This phenomenon has proven to have a material effect on proxy voting and should be primarily resolved through the implementation of a more transparent share-ownership infrastructure. To avoid over-voting, some broker-dealers have adopted methods of allocating votes among their customers that can result in beneficial owners casting more or fewer votes than they are entitled to cast. Vote tabulators follow numerous procedures for accepting votes from DTC participants. The scenarios described in the Release covering the reconciliation and allocation methodologies demonstrate the complexity of share tracking throughout the settlement period, and indicate a need for the disclosure of vote allocation and reconciliation procedures.

Vote Tabulation & Confirmation

SBA staff believes that the voting process should be an accurate, transparent, and efficient process. During the last 30 years, there has been a tremendous advance in digital technology and global integration. We believe that a transition towards an electronic proxy voting system, while not complete, has enhanced the efficiency of the system, while maintaining shareowner's anonymity, through automation. Furthermore, the fulfillment of a transparent electronic voting system could facilitate better vote tabulation and increase investor confidence in the voting process.

All proxy votes need to be accurately tabulated. SBA staff believes that votes properly cast should be correctly tallied. In conjunction with this view, we also believe the proxy voting system should provide for end-to-end vote confirmation. End-to-end voting integrity provides both companies and shareowners assurance that instructed votes were included in final vote tabulations. Currently, shareowners do not have the ability to confirm that their votes have been cast and tabulated as instructed in an end-to-end fashion. Transfer agents often provide vote tabulation services, with independent third party(s) certifying voting results, both of which are selected and paid for by the issuer with little to no line-item reporting made to investors.

Although the current "voting chain" is complex and presents challenges for achieving vote confirmation, they are not insurmountable. SBA staff views the possible design and creation of unique identifiers or codes for beneficial owners as real options and warrants further study. Such identifiers could be used to establish an audit trail through which beneficial owners and companies could automatically confirm vote instructions, share count, and tabulation accuracy. There should be standard rules applied to vote tabulation and disclosure of the methodology used by each firm providing such services, and should likely be administered by a central entity such as the Depository Trust Company (DTC). In addition, we believe the tabulation and vote allocation processes should be subject to regular external audits.

² Since 2007, the SBA has disclosed its proxy voting records, identified proxy advisory firms used during the latest fiscal year, benchmarked proxy voting decisions, and related corporate governance activities on its website and within the SBA Corporate Governance Annual Report.

Another issue many investors are frustrated with is the inability to vote two separate proxy cards (ballots) in proxy contests. Most issuers have not allowed shareowners to support director candidates from both the management and dissident proxy cards simultaneously. In the SBA's own experience, there have been only a few isolated cases when we've been given the procedural capability to split our votes among some of management's nominees and some of the dissident nominees—normally exhibited during close votes when one (or more) of management's candidates appear to be failing to achieve shareowner approval. Investors would most likely prefer consistent and standardized rules allowing voting to take place across both management and dissident proxy cards. We urge the Commission to further examine such procedural voting discretion.

Advance Voting Instructions

The Council of Institutional Investors (CII) released a study on client directed voting (CDV) in August 2010, which evaluated the various components of advanced voting instructions.³ The study concluded that no conceived variation of CDV would adequately address the main obstacle of investor education – convincing retail beneficial owners of the significance of their voting rights. Under most CDV models, retail investors would set voting instructions ahead of annual meetings and prior to proxy votes being cast. The current proxy framework, in contrast, is based on rigorous and timely disclosure to investors. Without such information, investors are simply not able to make informed voting decisions on material financial matters, whether voting on board of director nominees, executive compensation plans, or major corporate mergers.

SBA staff views most CDV model(s) as interdependent on numerous other reforms the Commission is working to address, and are concerned that a rigid form of CDV—in which shareowners must choose among always voting with management, always voting against management, always abstaining, or always voting in accordance with a third-party—may not be able to fully capture shareowners' preferences under most circumstances. A more nuanced CDV (referred to by some market participants as “open CDV”) model should include the ability to revoke advance voting instructions, require periodic reaffirmation of advance instructions, and allow for directed voting to retail investor-oriented third parties.⁴ SBA staff favors the potential for shareowners to direct their proxy and/or implement advance voting instructions to third-party platforms. For example, retail investors could be allowed to assign their proxy and voting rights to one or more other investor(s) (or group of investors) to vote specific types of proposals.⁵ Many organizations are moving in this direction already, and a few have implemented systems with the capability, including ProxyDemocracy, Broadridge, and Moxy Vote.

NOBO/OBO

Under the current share ownership structure, few beneficial owners are the direct holders of record. Rather, a multi-level chain of custodial ownership operates to separate the record and beneficial owner. This system not only inhibits a company's ability to communicate with its shareowners, but also incurs fees that intermediaries charge to serve as custodians, which are ultimately passed on to investors. SBA staff supports efforts to reform the Objecting Beneficial Owner (OBO)/Non-Objecting Beneficial Owner (NOBO) system in a way that encourages more transparent stock ownership while still allowing an option for investors to maintain their anonymity.

³ “*Client Directed Voting: Selected Issues and Design Perspectives*,” by Alan L. Beller, Janet L. Fisher, and Rebecca M. Tabb is available at: <http://www.cii.org/UserFiles/file/resource%20center/publications/CII%20White%20Paper%20-%20Client%20Directed%20Voting%20August%202010.pdf>.

⁴ See “*An Open Proposal for Client Directed Voting*”, available at: <http://blogs.law.harvard.edu/corpgov/2010/07/14/an-open-proposal-for-client-directed-voting/>

⁵ The SBA has partnered with ProxyDemocracy.org since 2008, integrating SBA proxy voting information on specific company ballots, on a shared internet platform. ProxyDemocracy.org collects and displays the actual votes from several large pension funds and other institutional investment organizations.

The Council of Institutional Investors (CII) recently commissioned an independent study, released in February 2010, to investigate the OBO/NOBO distinction and its implications.⁶ The study concluded that the OBO/NOBO system should likely be eliminated. The study identified two steps designed to promote greater transparency around shareowner lists and opportunities for direct communications by shareowners and companies: 1) elimination of the OBO/NOBO distinction through a phased implementation starting with a mandate to make NOBO the default status and charging a fee to shareowners who wish to maintain anonymity via OBO status; and 2) remove, or decrease, current restrictions on the ability of companies and shareowners to distribute proxy materials and solicit proxies directly, thereby streamlining the process for both companies and shareowners to obtain shareowner lists. SBA staff believes changes to the OBO/NOBO mechanism would encourage competition in the proxy distribution space and likely decrease aggregate costs. As well, suggestions made by the Shareholder Communications Coalition and the Business Roundtable offer details on how direct communications with investors could be implemented without disrupting current arrangements for settlement, clearance, and record-keeping.

Voting Power and Economic Interest

Through the use of various hedging strategies possible with complex financial instruments, investors may have voting power which exceeds their economic interest in a company. Therefore, a shareowner can hedge away the change in value of a company's stock in order to isolate only their voting power. The practice of "empty voting" can be related to the practice of securities lending, whereby securities lending markets can host a market for votes.⁷ Empty voting is asserted to be a tactic supported by asymmetric information in the securities lending market. We have reviewed our own lending volumes over the record dates of meetings with significant voting items and have found evidence that the shares on loan are abnormally high around 'contested' or important meetings. In 2007, the SBA provided commentary to the Commission regarding the issue of securities lending and its impact on the effectiveness of proxy voting.⁸

At the time, SBA staff viewed the primary issue to be poor disclosure—as most shareowners are not aware of the record date for upcoming votes, nor are they informed of the upcoming voting items to be ratified on the proxy. The view of SBA staff has not changed since then and continues to focus on the disclosure of record dates and ballot level detail in order to promote fairness and provide investors with full access to information. In line with these views, SBA staff supports: 1) full disclosure of shareowner meeting agenda sufficiently ahead of the record date (at least 10 days prior to the record date) to enable investors the ability to recall loaned shares; 2) investor certification of "full economic interest" in the shares being voted; and 3) prohibiting (or otherwise restricting) voting rights not commensurate with an investor's "net long position." The proxy voting disclosures by investors themselves should include both the actual number of shares voted as well as the number of shares which the fund did not vote (because of securities lending activities, or other factors).

Dual Record Dates

A dual record date framework, although not common or mandated, allows the use of one date to assign the right to vote shares and a different date used for meeting notice and communication purposes. SBA staff supports further evaluation of the use of dual record dates as long as its practice does not inhibit proxy voting or complicate the voting process. The dual record date system allowable under Delaware state law may be the preferred model, but there are likely practical challenges to the implementation of record dates with very close proximity to meeting dates (e.g. less than 20 days). For such record dates close to the annual meeting date, it may be appropriate for

⁶ "The OBO/NOBO Distinction in Beneficial Ownership: Implications for Shareowner Communications and Voting," by Alan L. Beller and Janet L. Fisher, available at: <http://www.cii.org/UserFiles/file/CII%20White%20Paper%20-%20The%20OBO-NOBO%20Distinction%20in%20Beneficial%20Ownership%20February%202010.pdf>.

⁷ See "Vote Trading and Information Aggregation" by Susan E. K. Christoffersen, Christopher C. Geczy, David K. Musto, and Adam V. Reed, January 2007; and also "Does Proxy Voting Affect the Supply or Demand for Securities Lending?" by Renee Aggarwal, Pedro A.C. Saffi, and Jason Sturgess, October 2010.

⁸ SBA letter to the SEC Division of Corporate Finance dated February 5, 2007.

investors who purchase shares “late” to obtain proxy information online. As well, it is clear that temporary, short-term ownership changes resulting from tax-driven dividend capture strategies reduces vote participation when a dividend record date coincides with a voting record date.

Data-Tagging (XBRL)

SBA staff strongly supports the use of standardized data-tagging for proxy related materials and voting results as a means of increasing transparency and expanding shareowners’ ability to track governance practices, compare practices among peers, make informed voting decisions, and follow the results of shareowner meetings. We urge the Commission to adopt a uniform vote tracking procedure covering all brokers, banks, custodians, and intermediaries. The implementation of data-tagging for proxy-related materials and voting results would require careful attention to how the data is used by investors.

In addition to proxy filings, data-tagging could be applied to other investor reporting requirements, such as N-PX disclosures. The current reporting template does not lend itself to easy or comprehensive analysis of N-PX voting information. The difficulty of collating voting data among disparate N-PX filers and the cumbersome structure of filed information has been a concern among many governance research firms and asset owners for several years, including The Corporate Library, AFSCME, and ProxyDemocracy. Currently, investors have great difficulty searching for and locating specific fund filings within the EDGAR platform. The implementation of a standardized N-PX reporting template, with some form of machine-readable data-tagging, would certainly allow more thorough and efficient investor analyses.

Thank you for your consideration of these significant improvements to the proxy voting process and related regulatory oversight. If you have any questions, please contact Michael McCauley, Senior Officer—Investment Programs and Governance, at (850) 413-1252, or governance@sbafla.com.

Sincerely,



Ashbel C. Williams
Executive Director & CIO

cc: Governor Charlie Crist, as Chairman of the SBA
Chief Financial Officer (CFO) Alex Sink, as Treasurer of the SBA
Attorney General Bill McCollum, as Secretary of the SBA