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NYSE EURONEXT

VIA E-MAIL AND FEDERAL EXPRESS

July 9, 2013

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: SR-NYSE-2013-07

Dear Ms. Murphy:

NYSE Euronext, on behalf of New York Stock Exchange LLC ("NYSE" or the "Exchange"), submits this letter in response to the Order issued by the Securities and Exchange Commission (the "SEC" or the "Commission") in Release No. 34-69622, May 23, 2013, instituting proceedings to determine whether to disapprove the proposed rule change contained in the above-referenced filing (the "Order"). In its filing the Exchange proposed to amend NYSE Rules 451 and 465, and the related provisions of Section 402 of the NYSE Listed Company Manual, which provide a schedule for the reimbursement of expenses by issuers to NYSE member organizations for the processing of proxy materials and other issuer communications provided to investors holding securities in street name.

In the Order, the Commission questions whether the Exchange has provided adequate justification for material aspects of the rule change proposal. The Order details instances in which there is concern that the Exchange has not adequately or clearly explained the basis for certain of its conclusions. The Exchange believes that the work done by its Proxy Fee Advisory Committee ("PFAC") together with additional work done by Exchange staff, developed adequate justification for the proposals. The Exchange will expand upon the explanations previously provided in the rule filing and in the Exchange's letter dated May 17, 2013 responding to comments, to demonstrate this to the Commission.

The Exchange is also attaching a transcript of a June 4, 2013 interview of Paul Washington, who chaired the PFAC, in which he describes the reasoning and the approach taken by that committee.[1]

The PFAC was a body formed by the Exchange, but comprised of independent representatives from the issuer, broker-dealer and institutional investor community. The PFAC spent some 18 months learning what is involved in proxy distribution from a number of the actors involved in the process, analyzing various fee scenarios and then applying the lessons learned to make sure that the fees are allocated among the issuer community as fairly as possible. The PFAC utilized

[1] The video of this interview is available at https://www.boardmember.com/BRC.aspx?taxid=2766&id=9887

information obtained from Broadridge – it would be irresponsible not to – but it also confirmed this information with others involved in the area, and supplemented the information from Broadridge with information from other distribution providers and from brokerage firms.

One overriding issue that the Exchange wishes to address at the outset relates to the question of industry costs. The Order states that "neither the Exchange nor the PFAC have articulated a sufficient analysis of Broadridge's costs of providing proxy processing services, including with respect to issuers of various sizes, or of the costs incurred by broker-dealers that may go beyond the services provided by Broadridge." [2]

While the PFAC and the Exchange did in fact investigate and analyze those costs, the Exchange believes that what is a "sufficient analysis" in this regard must be viewed in light of the history of the proxy fee rules and the SEC Rule which has for many years been the basis for such fees. As the Order states, "this reimbursement structure stems from SEC Rules 14b-1 and 14b-2 under the [Securities Exchange] Act, which impose obligations on companies and nominees to ensure that beneficial owners receive proxy material and are given the opportunity to vote. . . . Under these rules, companies must pay nominees for reasonable expenses, both direct and indirect, incurred in providing proxy information to beneficial owners. The Commission's rules do not specify the fees that nominees can charge issuers for proxy distribution; rather, they state that issuers must reimburse the nominees for 'reasonable expenses' incurred."[3] The Order goes on to note that the Commission left the determination of reasonable costs to the self-regulatory organizations ("SROs") because they were deemed to be in the best position to make fair evaluations and allocations of costs associated with these rules.[4]

As proxy distribution processes evolved, both at firms and at intermediaries, the costs incurred in the proxy distribution process have not typically been segregated from other costs incurred by these firms in their businesses. As technology developed and computer processing became a part of any large data processing task, development costs and technology maintenance costs were bundled together with other costs across a broad range of areas rather than tracked individually so as to enable a determination of what costs, or portion of costs, should be allocated to the reimbursable activity of distributing proxies to street name shareholders. And as the outsourcing of significant amounts of these activities became more common throughout the 1980's and 1990's, there were no rules dictating the cost accounting to be followed by the entities to which such work was outsourced and no separate requirement that these costs be accounted for independently. The result today, the PFAC found from conversations with various brokerage firms as well as with the intermediaries Broadridge and Mediant, is that there is no common methodology for tracking these costs, nor do these entities segregate these costs from the cost of other similar processing activities that are not reimbursable by issuers. It is also worth noting that the PFAC estimated that issuers spend approximately $200 million in aggregate on fees for proxy distribution to street name shareholders during a year, while information from both

[2] Order at page 55.

[3] Order at page 3.

[4] Order at n. 9.

Broadridge and Mediant reflect that revenues from NYSE-set proxy fees are a minority of their total revenues.

This is why the PFAC and the Exchange "judged that it would likely be impossible and certainly not cost effective, to engage an auditing firm to review industry data for purposes of the Committee's work."[5] However, the PFAC did study available materials that allowed it to conclude that the fees it proposed did constitute a reasonable reimbursement of the industry's costs for proxy distribution to street name accounts.

Given that it is conducting a business, the PFAC accepted that it was appropriate for Broadridge to make a reasonable profit. There was available to the PFAC public information showing Broadridge's pre-tax margin on its ICS segment, the business segment that includes the proxy processing activities. That margin has varied within a 14 – 16% range during Broadridge's time as an independent public company (commencing in 2004). At the PFAC's request Broadridge also supplied information regarding the margins of other firms in comparable businesses, such as transaction processing firms (e.g., Visa), financial processing firms (e.g., Fiserv), other processing firms (e.g., MSCI) and securities industry infrastructure firms (e.g., Computershare). Broadridge's margin was consistent with, and in most cases was significantly lower than, these other businesses. The PFAC found this credible evidence that the profit being earned by Broadridge on this business segment was reasonable. The PFAC also reviewed independent analyst reports on Broadridge, and found nothing in such reports to suggest that Broadridge's ICS segment was responsible for unusual or outsized profits. Nothwithstanding this initial test, the PFAC continued to consider the reasonableness of the fees and how they contribute to Broadridge's overall profitability throughout its review.

While it is common to bemoan the lack of substantial competition for Broadridge in providing intermediary proxy services to banks and brokers, the modest margins, when combined with the substantial infrastructure investment required to participate in the business, are a likely explanation for Broadridge's dominance. That is why the recent recapitalization of one of the small competitors, Inveshare, is good news for potential increased competition. Having secured the active backing of Computershare, Inveshare will have both capital and the distribution infrastructure (given Computershare's significant transfer agent business) to present a strong alternative to Broadridge as banks and brokerage firms evaluate their outsourcing arrangements going forward. More competition in the intermediary space can only help insure that profits remain at no more than a reasonable level, and will in the future provide additional sources of information regarding the appropriateness of the NYSE-enacted fees.

Of course not all the proxy fee revenue is retained by the intermediaries – certain firms have negotiated arrangements with Broadridge in which a portion of the proxy fee revenue collected by Broadridge in connection with distributions to their street name clients is returned to the brokerage firm. The PFAC and the Exchange looked at the activities performed by the firms

[5] SEC Release No. 34-68936; SR-NYSE-2013-07 (February 15, 2013)("NYSE Rule Filing) at page 41. The Exchange's Proxy Working Group in 2006 recommended that the NYSE engage an independent third party to analyze what is a reasonable amount for issuers to be charged in proxy fees and to commission an audit of industry costs and revenues for proxy mailing. However, as the Exchange investigated how this might be done, the difficulty and expense involved became evident, and no such exercise was in fact undertaken.

beyond what is outsourced to Broadridge, and requested information from SIFMA on brokerage firm costs. This information allowed the PFAC and the Exchange to be comfortable that the portion of the proxy fees that were returned to the firms was not in excess of the industry's cost to provide proxy distribution and processing services. This investigation will be described later in this letter, most particularly in the last section regarding the "cost recovery payments" retained by the firms.

We would now like to respond to other issues highlighted in the SEC Order:

1. The SEC described the PFAC as relying "substantially on information provided by Broadridge", and expressed the view that they "did not look beyond to obtain a clearer understanding of changes in the cost of the proxy process."

It is certainly true that the PFAC and the Exchange utilized information from Broadridge – doing so is unavoidable given the very large role that Broadridge plays in the proxy distribution process. However, the PFAC and the Exchange did not simply accept uncritically positions taken by Broadridge. There was instead a healthy dialogue and "push back" to allow the PFAC to be comfortable that it could rely on the information it was given. The PFAC requested that Broadridge provide it non-public financial data, but Broadridge declined. Nonetheless, Broadridge was otherwise forthcoming with the PFAC and described at length their processes, and provided the PFAC with the detailed task list that was included with the Exchange's rule filing as an appendix to the SIFMA survey. The concentration of issuer invoice information at Broadridge was also used by the PFAC to test the impact of various proposed changes to the fees on different segments of the issuer population. The PFAC requested that Broadridge run tests of various proposals, so that the PFAC could analyze and compare in some detail how different fee structures would impact the issuer population, assisting the PFAC in determining to its satisfaction that its proposals fairly allocated the fees among different size issuers.

The PFAC also met with representatives of Mediant, the other intermediary that has a modest number of broker-dealer customers. Mediant was also useful in describing the proxy processing business. The PFAC invited Mediant to provide it with financial information, but it did not.

The PFAC also spoke with representatives of several firms regarding their proxy processing operations – Bank of America Merrill Lynch, Citibank, Morgan Stanley Smith Barney, Fidelity's National Financial and Curian Capital. Representatives of the PFAC also met with a working group of broker-dealers organized by SIFMA as well as a number of other participants in this process.[6] Finally, at the request of the Exchange SIFMA conducted a survey among a representative group of its members to demonstrate that costs incurred by members beyond the cost of outsourcing activities to Broadridge is consistent with the aggregate amounts paid by Broadridge to the brokers in "cost recovery payments". SIFMA utilized a representative sample of 15 firms covering 6 tiers of firms based on the number of equity positions processed per firm. The firms provided information about the costs they incur as part of the proxy distribution

[6] While we are emphasizing here the PFAC's study of industry processes in effecting proxy distribution to street name investors, the PFAC also met with a variety of issuers, and with other organizations with views on the proxy distribution process, such as Computershare, the Securities Transfer Association and MoxyVote.

process. While this information was subject to the same difficulties described above attendant to surveying cost information in a context where no cost accounting treatment is prescribed, and where firms have a varying mix of businesses and do not account for costs or allocate fixed/overhead expenses in any common way, it served as a representative study for the PFAC to help support the information Broadridge was providing. It also supported the notion that there were costs associated with the proxy distribution process beyond that incurred by Broadridge that the firms experience and for which they are not reimbursed.

2. What was the basis on which the PFAC determined to utilize five tiers for the basic processing fees? What are the "economies of scale" that the Exchange refers to?

The PFAC concluded that there were economies of scale in serving large issuers – just as the predecessor committee did in the 1990's. The economies of scale exist because in any proxy distribution job there are certain costs – usually referred to as "set-up costs", which will be incurred with respect to each job, regardless of whether the job involves a large number of street name accounts, or a small number. In many similar kinds of work, such as printing jobs, pricing will include a flat "set-up" fee or perhaps a minimum, as well as a "per-item" charge. The NYSE proxy fees, however, are all charged on a per account basis, so a job that distributes to only a relatively small number of accounts will generate a relatively small fee, which the PFAC understood from Broadridge often does not cover the "set-up" cost involved.

The PFAC requested and obtained from Broadridge a description of the major segments of activity involved in proxy processing.[7] That document described six activities – Event Identification, Data Aggregation, Preference Management, Material distribution, Client Service and Vote Processing and Issuance. Broadridge reports that there is significant infrastructure involved in each of these individual activities, providing for peak capacity, data security, disaster recovery, data accuracy and record retention, all of which have high components of fixed cost. Within each activity there are varying amounts of fixed and variable cost. Event Identification is almost entirely related to an issuer's job rather than to its number of shareholders. The tasks included within Event Identification include meeting job set-up, creation of the VIF, special instructions provided by the issuer and a master security data base. Data Aggregation includes tasks which have both fixed and variable cost characteristics – the development and operation of the communications channels between Broadridge and its 900 bank and broker clients, creating and maintaining an issuer event data base for nominees, monitoring of responses from nominees and reporting of these responses to issuers.   Material Distribution, Client Service and Vote Processing all include both fixed and variable cost tasks. Unlike these other costs, Preference Management tasks are largely variable cost in nature, but they also are intended to be reimbursed by Preference Management fees, rather than by the basic processing fees.

The PFAC was informed that neither brokers nor Broadridge normally break their costs into fixed and variable components, but that Broadridge has studied this issue and concluded that that there is a high component of fixed cost – as much as 50-60% in certain functions. Even a conservative estimate that fixed costs make up 25% of total costs indicates that neither the

[7] The document was provided to the PFAC and the Exchange in February 2011. It was included in the NYSE Rule Filing as Appendix 2 to the SIFMA survey, included in Exhibit 2 to the filing.

current nor the proposed proxy fee schedule fully reflects the benefits of economies of scale when providing services to large issuers. Structuring the basic processing fees to cover a 25% fixed cost component would result in increases for Tier I (small) issuers as a group of more than two and a half times the current fees. Viewed another way, current fees do not recover the costs of approximately 75% of the jobs processed in a given year (jobs of 1 to 10,000 positions, or Tier I as proposed).

A consequence of the traditional approach in which all processing fees are based on the number of accounts served is that most jobs are processed at a loss, but reimbursements in the aggregate are reasonable because the largest jobs provide the needed subsidy. The current two-tier and the proposed five-tiered structure for basic and supplemental processing fees is an effort to more fairly allocate fees to issuers whose jobs are not scalable from issuers whose jobs are scalable. As noted above, however, both the PFAC and its predecessor committees have avoided tiering that would fully allocate based on economies of scale because of their belief that it would not be appropriate to impose large fee increases on the smallest issuers. The PFAC requested and reviewed numerous pricing scenarios from Broadridge to ensure small issuers were not unduly impacted prior to agreeing on the five tiers proposed.

The PFAC did believe that it was appropriate to correct the deficiencies in the current "cliff" tier arrangement. As explained in the filing, the current fees make a simple binary distinction between Large and Small Issuers,[8] where the Large Issuer pays a reduced rate on all accounts holding its securities, not just those over a certain number. This pricing schedule means that there can be a significant difference in the overall processing fee paid by an issuer held by 199,000 street name accounts versus that paid by an issuer held by 201,000 accounts. Of course, the number of an issuer's street name accounts varies from year to year, so an issuer crossing this line from one year to the next will confront an unwelcome (and to the issuer, unpredictable) volatility in its proxy fees. So the PFAC wished to develop a more equitable tiering arrangement, in which fees would decline not for all accounts in issuers of a certain size, but where the same price would apply to the first tier in all companies, a reduced price to the second tier in all companies, and so on. In developing the five tiers used in the proposal, the PFAC considered and analyzed a number of scenarios, including scenarios with more than and fewer than five tiers. Scenarios with between two and four tiers were less effective in removing the distortions of the current cliff fee structure. Scenarios with more than five tiers, including those with sub-categories within the proposed five tiers, added a level of complexity to the fee rules that the PFAC considered undesirable.

The impact of the five tiers was tested against several representative samples of issuers, and the initial five tier approach was further amended at the PFAC's direction to ameliorate the increases projected for the tier one issuers. As a final check regarding the propriety of the proposed tiers, the PFAC had secured from Broadridge the estimate that overall under the current fees issuers with 100,000 or fewer accounts paid approximately 38% of proxy processing fees, issuers owned by more than 100,000 up to 500,000 accounts paid approximately 30% of such fees, and issuers owned by more than 500,000 accounts paid approximately 32% of the fees. Estimates of the

[8] 200,000 accounts was used as the break point in 2001 because at the time that was the midpoint among all issuers distributing proxies. The PFAC was informed in April 2011 by Broadridge that the midpoint had moved to approximately 290,000 positions.

impact of the tiered prices contained in the proposal were that such proportions would continue, which the PFAC considered to be consistent with its goals and to represent a fair allocation among the issuer population.

3. Why is the tiered approach not also appropriate for the preference management fee?
The PFAC examined this issue, and determined not to propose to tier the preference management fees for several reasons.

First of all, based on the detailed description of the activities involved in this task, it appeared to have fewer economies of scale than the other processing activities. Preference management processing was characterized by work that was related to each preference record, which is updated on a daily basis, rather than work triggered by a proxy job. Secondly, as described in more detail below, the PFAC determined to distinguish between managed accounts and other accounts in terms of the amount of the preference management fee. Having what are in effect two types of preference management fees would make tiering those fees more complex. The PFAC did ask Broadridge to model a tiered approach for preference management fees, but determined that it was too complex, especially in light of the fact that the basic processing fees were being tiered. This, combined with the relatively low quotient of "set-up" costs related to preference management fees, was the basis for the PFAC determination to avoid tiering the preference management fees. The proposed preference management fee of 32 cents is intended to replace the current 50/25 cents charged to Small/Large Issuers. Of course, the aggregate amount of preference management fees is reduced considerably by the proposal to cut in half (to 16 cents) the preference management fee on managed accounts.

4. Questions related to the treatment of managed accounts:

Q. The rational for the lower preference management fee for managed accounts is that such accounts benefit both issuers and brokers, which justifies having issuers and brokers "share", in effect, the preference management fee. Issuers benefit from managed accounts in the proxy context because almost all account holders delegate voting to the manager, and managers typically elect electronic delivery and vote much more frequently than the average retail investor. But how do brokers benefit from managed accounts in this context?

A. The benefit to brokers is not a benefit related to proxy processing, but rather refers to the fact that the managed account is a product type that has been increasingly popular as an "asset gathering" strategy for firms, providing fee income to the firms and permitting them to lessen reliance on commission income. The benefit to issuers in the proxy context is an incidental attribute of a product type marketed by the brokerage industry because of the perceived advantages of the product for both brokerage firms and investors. As a result, the PFAC believed it appropriate to differentiate between suppressions secured as a result of the type of account involved (i.e., a managed account), compared with suppressions secured because an investor with a non-managed account has agreed to electronic delivery or accepted householding of multiple accounts at the same address. Those latter types of suppressions benefit only issuers, with no identifiable benefit to the broker, other than payment of a preference management fee which is meant only to reimburse the broker's costs.

Q. Why are managed accounts treated differently only for purposes of the preference management fee, and not the basic processing fees as well?

A. The answer is twofold. First of all, managed accounts are individual accounts (SEC rules require managed accounts to be treated as such, to distinguish them from investment companies), and are processed as such. More importantly, however, the issue the PFAC was dealing with was whether the nature of the managed account justified distinguishing it from other accounts in terms of the preference management fee applied. The discussion was focused on the relative fairness of imposing a fee triggered by suppression of paper delivery for an account where the suppression appeared to be more a consequence of the nature of the account than an effort made to suppress paper delivery. Because the focus was on the separate suppression fee, the PFAC directed its attention to adjusting that fee; the basic processing fee was not a focus of the discussion.

Q. Why was the five share threshold chosen for the proposal that managed accounts below that level would incur no fee?

A. As explained in the filing, the PFAC was concerned with the proliferation of managed accounts containing a very small number of an issuer's shares, typically resulting when a managed account is offered with a relatively low investment minimum. This was apparently a concern even in the 1990's when the incentive fees were being developed, and led to the custom that was followed of not charging for "wrap accounts". Unfortunately, this approach became less effective over time given the lack of a definition of the term "wrap account", in addition to being problematical because it was not codified in the proxy fee rule. The PFAC searched for an approach that would deal more effectively with this issue.
A more precise alternative to the "wrap account" approach which the PFAC found attractive was to specify that no fees would apply to managed accounts holding fewer than a specified number of an issuer's shares. The question was what number of shares to specify. The PFAC obtained from Broadridge information showing that among managed account positions between 1 and 500 shares (which constituted 89% of all managed account positions), the average position was 91 shares, and median position size was approximately 50 shares. The basic question was at what point did the benefit to an issuer in terms of shares voted become so minimal as to justify charging the issuer nothing for processing the account. The PFAC was also mindful of the overall economic impact on proxy fees, not wanting to have a disparate impact from this one item. Accordingly the PFAC considered setting the bar at various points from a fractional share to 5, 10, 15, 20 and 25 shares, and obtained estimates of the economic impact of each of those set points. In the end, there was consensus at a level of five shares. The estimated impact on aggregate proxy fees was considered relatively modest (approximately $4.2 million), and it seemed clear that the voting benefit of five shares or less was limited, so say the least. This was a reasoned judgment by the PFAC, but one that was made after careful consideration of alternatives.

5. Since some brokers are able to negotiate with Broadridge to obtain proxy processing services at a price less than the aggregate fees collecting for servicing their accounts, why shouldn't the excess be passed on to issuers?

Just as there are economies of scale in processing a proxy distribution for a large issuer, there are economies of scale earned by the intermediary when it secures the account of a broker with a large number of street name accounts. Broadridge experiences economies of scale when it is able to spread its fixed costs over a greater amount of business, and a firm with a large number of accounts is a more attractive client to Broadridge (or any intermediary) than one with fewer accounts. The same economies of scale existed when firms did these distributions without an intermediary – the larger the firm, the more business over which it could spread its fixed costs.

While the maximum fees are set by the Exchange rules, the one area in this process where a market negotiation occurs is the arm's length bargaining between Broadridge and the nominees (banks and brokers). Those brokers that are the most attractive clients are able to extract from Broadridge more favorable terms than the smaller firms, and Broadridge is able to "afford" to give those terms because the per account pricing means that the larger account sources are subsidizing the provision of services to the smaller firms.

Information from Broadridge is that approximately 200 of its 900 bank/broker clients receive "cost recovery" payments. Since all firms have to incur at least some costs related to proxy distribution beyond the cost of retaining Broadridge, the 700 who are receiving nothing from Broadridge (i.e., who allow Broadridge to retain the entirety of the proxy fees generated by distributions to their accounts) are by definition not being fully reimbursed. Those that do receive payments from Broadridge are obviously those with the larger account populations, and who are most likely to have more sophisticated operations and greater costs of the type articulated in Appendix 1 to the SIFMA survey.[9] That survey demonstrated that on an industry basis, brokerage firms are not receiving reimbursement in excess of the costs they expend.[10]

This issue – that a one-size-fits-all fee schedule will have winners and losers – has been present in the proxy fee context from the beginning, and has apparently been acceptable to the industry and the SEC for that entire period. Given that a different approach seems not to be feasible without a detailed, utility-type fee structure, the Exchange submits that there is more than adequate justification for the rules as currently proposed.

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The Exchange is pleased to have the opportunity to submit this additional explanation to the Commission in support of the rule filing. We would also be pleased to answer any other questions that the Commission or the Staff may have.

Very truly yours,

Janet McGinness

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[9] As noted above, the SIFMA survey and its appendicies were included in Exhibit 2 to the Exchange's rule filing.

[10] We note that in the recent comment letter dated June 18, 2013 filed by Inveshare, that intermediary stated its view that "Broker-Dealers have a significant amount of work when delivering proxy materials, even when engaging an intermediary, and in most cases the <u>maintained</u> cost recovery (the amount provided to the broker-dealer from the intermediary) does not adequately cover the expense incurred."

[00:00:00]

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[00:00:20]

DARLA STUCKEY: Welcome to *Governance Minutes*. My name is Darla Stuckey and today we are very happy to have Paul Washington with us, who is the Senior Vice President, Deputy General Counsel and Corporate Secretary at Time Warner. We are here today to talk about something that's very close to corporate secretaries' hearts, which is proxy fees, an auspicious time to talk about them because it is proxy season, and also because the SEC recently postponed yet again approval or disapproval on the NYSE proxy fee rule filing.

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I just want to say a little bit of background. Under the Dodd-Frank Act, there are some new procedures. So an

SRO rule filing that goes in has basically two 45-day periods in which comments can be given. Those two 45-day periods have passed. If the SEC still is not ready to approve or disapprove, they can kick it into another gear, so to speak, which is ask for more comment or do some sort of roundtable. That's where we are now.

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In that process, they have to say what the issues are. They did a lengthy filing, I think 60 pages, and talked about some of their concerns. So we're going to talk about those and what we can do next as issuers. But first I want to ask Paul if I got all that right.

[00:01:38]

PAUL WASHINGTON: You did indeed. You did indeed. And you're right. The latest SEC filing was something we haven't seen much of because it's just come out since Dodd-Frank.

[00:01:47]

DARLA STUCKEY: Right, I had never --

PAUL WASHINGTON: It was an animal I had not seen before. So, yes.

DARLA STUCKEY: Right. So let's start with the PFAC itself, commonly called PFAC, Proxy Fee Advisory Committee. How was it formed? How did you guys operate, and sort of how much time did you spend in your review? Give us an overview of the PFAC in the process, which started I guess in September of 2010?

[00:02:08]

PAUL WASHINGTON: Right. In the summer of 2010, the New York Stock Exchange pulled together this advisory committee consisting of issuers, brokers, others who are, you know, interested in the $200 million a year that issuers pay to have our proxy materials sent on by banks and brokers to the folks who hold in street name. So there is a lot of money involved here, not a lot necessarily at each company, but there is a lot of money involved.

So they pulled together this group of people from a variety of backgrounds. The majority of the PFAC was issuers, so actually -- and since we're the folks who are actually paying the fees, that seemed appropriate, but at the same time it shouldn't just all be dictated by the issuers.

[00:02:57]

We met -- held a series of meetings with pretty much anyone who wanted to meet with us. We heard from -- you know, we heard from issuers, we heard from Broadridge -- we heard from competitors to Broadridge. We heard from investors, a whole range of people, and we had a series of meetings finally issuing a report in May 2012, so a good sort of year-and-a-half of work went into it, and we tried to do a really thorough analysis of something that is a fairly obscure, technical, but nonetheless important -- important issue.

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What's really at stake here is having a system that gets our proxy materials into the hands of shareholders. That's -- and then having a system that then processes the votes and so forth appropriately. That system fundamentally works. We didn't want to do anything that would undermine it, but what we wanted to do was to make sure that the fees that pay for that system are appropriate.

DARLA STUCKEY: Right.

PAUL WASHINGTON: We can talk more about what went into that.

DARLA STUCKEY: Right. And just to back up a little bit or give a historical context, this is, at least in my lifetime or my known lifetime, right? This is the third or fourth iteration of this group.

PAUL WASHINGTON: Right.

[00:04:14]

DARLA STUCKEY: It seems to come about every four, five or six years. When I was at the NYSE, we -- Jim Buck ran a process. Actually, Ken Bertsch was involved in a process even before this. So this happens every few years, usually resulting in some tweaking of the fees. That was, I guess, the expectation this time, although I think you did a little more. You at least started with a set of goals that were articulated that I thought were pretty rigorous.

PAUL WASHINGTON: Well, thanks.

DARLA STUCKEY: Can you tell us what those were?

PAUL WASHINGTON: Sure. Yeah. This is one of those places where a lot of good work had been done by prior groups, but there isn't a sort of set formula for how to go about doing this. You know, you can go back and look at the records and the filings, but there wasn't -- we had to sort of come up with a template that we thought would be appropriate.

[00:05:01]

Of course, the main thing is we needed to make sure that the fees provided reasonable reimbursement for the costs of banks and brokers in handling our proxy materials and the voting. Of course, they in turn outsource a lot of this to Broadridge. So that was the primary thing, that we really wanted to make sure that we were providing reasonable reimbursement.

But there are things that go along with that that I think were somewhat more detailed criteria. The first thing is we didn't want to do anything that messed up the current system.

DARLA STUCKEY: First do no harm.

PAUL WASHINGTON: Do no harm. It works, right? So that was the first thing. Second, we thought that we should make the -- to make the fees more transparent. There's a lot of confusion when issuers get their bills.

[00:05:53]

DARLA STUCKEY: What is this?

PAUL WASHINGTON: What are we even paying for? And some of the things were misnamed in some ways, or at least the names have become outdated. So we wanted to make sure they were transparent.

[00:06:06]

We also along -- we wanted to make sure that the fees were fair and corresponded to the amount of work that was being involved with either a particular issuer or particular holder. So we wanted to make sure there was a correlation, they were fair, that there was a correlation between the work being done and the amount of the sort of specific sub-fees.

DARLA STUCKEY: Did you find any specific example of work being done --

PAUL WASHINGTON: Oh, sorry.

DARLA STUCKEY: -- that we were surprised about that cost more than you would have ever dreamed?

PAUL WASHINGTON: Yes.

DARLA STUCKEY: -- or that an issuer would have ever known?

PAUL WASHINGTON: Yeah, right.

DARLA STUCKEY: That's what Broadridge has always said. So I don't -- you know --

PAUL WASHINGTON: Oh, definitely. This whole thing was an education. But one of the things that a lot of us wondered about is, well, there are these incentive fees. That's for shifting over from paper delivery basically to electronic delivery. We thought, "Well" -- and most issuers did. "Well, okay, we've shifted over. Why are we still paying incentive fees? That just doesn't make sense."

[00:07:06]

Well, then we looked at the amount of work that Broadridge is doing. First of all, we realized that it's not a one-time thing. Once an investor has registered its preference in one way, whether it's for house-holding or electronic delivery and so forth, it's not just a one-time thing. Broadridge has to check that every year, a couple of times a year. So it runs through all these traps.

Then we discovered that actually the amount of money that correlates to the overall amount of money that's paid out for incentive fees -- what we now call preference management fees -- is actually a smaller percentage of the pie than the amount of work that actually is going into it. We didn't make things match exactly, but we did realize that a huge amount of the effort that Broadridge makes and banks and brokers make --

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DARLA STUCKEY: And it's what? Technology? Database management? What is it?

PAUL WASHINGTON: It's technology. It's all of that sort of stuff. It's also people's time. But a lot of it is managed electronically, but as you know, that's not cheap. It's not a one-time cost.

DARLA STUCKEY: Right.

PAUL WASHINGTON: So that was really eye-opening.

DARLA STUCKEY: So I didn't mean to cut you off, but as far as the transparency, the first do no harm.

[00:08:21]

PAUL WASHINGTON: You know, do no harm, reasonable reimbursement. We want it to be fair, more transparent. We wanted to facilitate retail voting to the extent possible. We also wanted to be sensitive in terms of not making such -- this goes with the doing no harm, but not making such radical changes that would have potentially unintended consequences because while there have been concerns about bills that issuers are paying, we were -- we were quite sensitive to the fact that if suddenly because we were trying to match the costs with the amount of work involved, if you were to do that fully, the cost to small issuers would skyrocket.

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DARLA STUCKEY: Right. We've heard this.

PAUL WASHINGTON: So we were very sensitive not to raise the costs for any category of issuer dramatically or lower them dramatically, for that matter, just because, you know, it wasn't -- that didn't seem fair and reasonable reimbursement to us. We didn't want to upset the apple cart that much.

So we were sensitive to that. We didn't want to, you know, have this group of people who were suddenly finding themselves disadvantaged in this area.

DARLA STUCKEY: Right. So the SEC in its latest filing, their response, they seemed to really have trouble with the fact that what sounded like maybe you didn't get all the information you needed or you didn't adequately discover what the costs were to process a proxy. I mean, how -- what do you say to that?

[00:10:02]

PAUL WASHINGTON: Right. Well --

DARLA STUCKEY: Ouch?

PAUL WASHINGTON: [LAUGHTER] No, look. It's a fair question and it's something that we on the committee ourselves really grappled with, which was how much information we should get to be able to make this assessment of whether we were providing reasonable reimbursement for costs.

There are a couple of models to take. There is the model that could be taken, which would be, call it a utility rate-setting model, where you've got a massive regulatory entity that goes through and combs through the books of everyone involved, in this case it would be a utility or a power company, to figure out exactly how much it costs to deliver power, all this sort of --

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DARLA STUCKEY: Buy the electricity and then deliver it. Right.

PAUL WASHINGTON: And all the overhead and all that kind of stuff. And then say in a sort of government-dictated way, "And here is your adequate return, your adequate profit." That has never, ever been the approach of the SEC, never been the approach of the NYSE.

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If someone wants to set up that whole regulatory oversight process, maybe they could do that. But what we were doing is working within the realm of the possible, and within that realm, we did everything we could to satisfy ourselves that the fees that we were proposing, the fee structure, was appropriate. So a few things to keep in mind; the fees we're proposing would overall lower fees by about 4%. That's despite the fact that since the last time the fees were set inflation has gone up 20%. We have been in a low inflation rate recently, but over the last 10 years, or whatever it's been --

DARLA STUCKEY: Right. Right.

[00:11:35]

PAUL WASHINGTON: The costs have gone up overall 20%. We also looked at Broadridge's publicly available financials and their margin in this area -- we did want to make sure that there was no sort of gross profit-taking or anything like that, right?

[00:11:50]

DARLA STUCKEY: I was going to say, were they making 30%?

PAUL WASHINGTON: No. It was 16%, and it's been going down to 14%. So it's actually declining margins in this area. So if the fees before had been reasonable that were approved by the SEC and set by the NYSE, why it seemed that given that, you know, costs have gone up, we're proposing fees that have gone down, we looked at the available information and nothing seemed to be off in terms of margins. We looked at the amount of work that Broadridge was doing and matched it up against the fees. Then we looked at independent analyst reports.

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You would think that if they thought that anyone, banks, brokers in terms of the money that they keep in this process or Broadridge were sitting on a gold mine, someone would have said it. And there was no -- there was literally no evidence of that. In fact, after PFAC was done with its work, the -- there was additional work done by the NYSE to see whether banks and brokers were somehow hugely profiting by this because sometimes they get some rebates back from Broadridge. And, in fact, if anything, they're incurring expenses that are not being, you know --

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DARLA STUCKEY: Reimbursed by them.

PAUL WASHINGTON: Reimbursed by issuers.

DARLA STUCKEY: I have heard that, but people don't believe that it seems like. Yeah.

PAUL WASHINGTON: We looked at the numbers just based on the sample. So I think everything indicates that the fees that have been proposed by the New York Stock Exchange to the SEC are a more reasonable reimbursement than what we have had --

DARLA STUCKEY: Had in the past.

PAUL WASHINGTON: -- had in the past.

DARLA STUCKEY: So Paul, what -- we don't have much time. What is the worst thing about the fact that this hasn't been approved yet, or that it may not get approved?

PAUL WASHINGTON: Well --

DARLA STUCKEY: What is the worst thing?

[00:13:29]

PAUL WASHINGTON: My hope -- my hope is that there may be some additional information that the New York Stock Exchange or others can produce to the NYSE -- to the SEC that will satisfy its concerns.

DARLA STUCKEY: Right.

PAUL WASHINGTON: I think in terms of, you know, did we do enough to figure out the right tiering, I think there is more information that can be shared there. I hope that issuers speak up because it would be great for the SEC to hear from issuers that they actually think that the new fees that the society set are better than the current ones.

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The worst thing that could happen, frankly, is that if the proposed fees are not approved and we're stuck with the old fee schedule, we as issuers will be paying too much. There will be people who will be paying a lot for managed accounts, where you can have tiny fractional shares and we are over -- we as issuers are overpaying for that. And you'll have other anomalies in the current fee structure.

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And frankly, those fees could go on indefinitely because there is no set requirement for the fees, as we started off with, to be updated.

DARLA STUCKEY: Right. Right.

PAUL WASHINGTON: So we would not have what I think is a better structure. We would be stuck with an old structure that people have been complaining about.

DARLA STUCKEY: Right.

PAUL WASHINGTON: So -- and might be stuck with it indefinitely. So I hope we're not there. I hope we can find our way through. I'm sure that all the other issuers who are on the PFAC will do everything we can to help make the case as well as we can.

DARLA STUCKEY: Okay. Well, it is tough, and I appreciate you being here. I hope the issuers listening will, you know, write to the SEC. They did reopen the comment period. Not clear if they're going to have a roundtable, but in any event, put in whatever comments you want, and thanks so much for being here, Paul. We've got to -- we've got a lot of work to do.

[00:15:08]

PAUL WASHINGTON: It's my pleasure, and thank you Darla.

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