

COMMENT LETTER

June 20, 2013

Additional ICI Comment Letter on NYSE Proposal Regarding Proxy Distribution Fees (pdf)

June 20, 2013 Elizabeth M. Murphy Secretary Securities and Exchange Commission 100 F Street, N.E. Washington, D.C. 20549-1090 Re: Additional Comments on NYSE Proposal Concerning Proxy Distribution Fees (File No. SR-NYSE-2013-07) Dear Ms. Murphy: The Investment Company Institute (“ICI”)¹ appreciates the opportunity to comment in response to the Securities and Exchange Commission’s order (“Order”)² instituting proceedings to determine whether to disapprove a proposed rule change (“Proposal”) filed by the New York Stock Exchange (“NYSE”) earlier this year. ³ The Proposal concerns proxy distribution fees—i.e., the fees that broker-dealers and banks are entitled to receive from issuers for forwarding their proxy materials to ¹ ICI is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of \$15.2 trillion and serve over 90 million shareholders. ² See Securities and Exchange Commission, Self-Regulatory Organizations; New York Stock Exchange LLC; Order Instituting Proceedings to Determine Whether to Disapprove Proposed Rule Change Amending NYSE Rules 451 and 465, and the Related Provisions of Section 402.10 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 and to Establish a Five-Year Fee for the Development of an Enhanced Brokers Internet Platform, SEC Release No. 34-69622 (May 23, 2013), 78 Fed. Reg. 32510 (May 30, 2013), available at <http://www.sec.gov/rules/sro/nyse/2013/34-69622.pdf>. ³ See Securities and Exchange Commission, Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing of Proposed Rule Change Amending NYSE Rules 451 and 465, and the Related Provisions of Section 402.10 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 and to Establish a Five-Year Fee for the Development of an Enhanced Brokers Internet Platform, SEC Release No. 34-68936 (Feb. 15, 2013), 78 Fed. Reg. 12381 (Feb. 22, 2013), available at <http://www.sec.gov/rules/sro/nyse/2013/34-68936.pdf>. Ms. Elizabeth M. Murphy June 20, 2013 Page 2 beneficial owners who hold shares in “street name.” It is based, in large part, on recommendations issued last year by an industry working group, the Proxy Fee Advisory Committee (“PFAC”).⁴ ICI submitted a comment

letter when the SEC published the Proposal for public comment because, as discussed in that letter, the registered investment companies (“funds”) we represent have a strong interest in the structure and amount of fees charged for the distribution of proxy and related materials to beneficial shareholders.⁵ Our comment letter expressed the view that there is a need for a rigorous, independent review of the current system that includes, among other things, a thorough analysis of actual costs involved. We stated that, at a minimum, there should be further analysis of the proxy fees paid by funds and how the proposed changes would affect those fees. Notwithstanding the NYSE’s response to comments on the Proposal,⁶ we continue to hold these views. We were pleased, therefore, that the SEC decided to institute proceedings to determine whether to disapprove the Proposal. As the Order indicates, the Proposal’s analysis leaves open important questions about whether the Proposal meets the statutory standards that apply to self-regulatory organization (“SRO”) rulemaking.⁷ As discussed below, we do not believe that it does. Accordingly, we urge the SEC to disapprove most of the Proposal and to call for an independent review of proxy distribution fees.

Discussion The Order discusses the legal and policy issues raised by the Proposal and identifies numerous weaknesses in the information the NYSE provided to support the proposed rule changes. We share the SEC’s concerns both as a general matter and with respect to particular aspects of the Proposal. ICI strongly commends the SEC for its careful study of the Proposal and serious consideration of the concerns expressed by many commenters, including ICI. Given that millions of fund investors ultimately bear the costs of distributing fund proxy materials, we believe it is entirely appropriate for the

⁴ See Recommendations of the Proxy Fee Advisory Committee (May 16, 2012) (“PFAC Report”), available at https://usequities.nyx.com/sites/usequities.nyx.com/files/final_pfac_report.pdf. ⁵ See Letter from Dorothy M. Donohue, Deputy General Counsel – Securities Regulation, Investment Company Institute, to Ms. Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, dated March 15, 2013, available at <http://www.sec.gov/comments/sr-nyse-2013-07/nyse201307-14.pdf>. ⁶ See Letter from Janet McGinness, EVP & President, NYSE Euronext, to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, dated May 17, 2013, available at <http://www.sec.gov/comments/sr-nyse-2013-07/nyse201307-29.pdf>. ⁷ See, e.g., 78 Fed. Reg. at 32522 (stating that “significant questions exist as to whether the Exchange has provided adequate justification for material aspects of its proposal such that the Commission can make a determination that the proposal is consistent with the [Securities Exchange] Act.”). Ms. Elizabeth M. Murphy June 20, 2013 Page 3 SEC to hold the NYSE to a high standard of analytical rigor in making the case that the Proposal is consistent with applicable requirements of the Securities Exchange Act of 1934 (“Exchange Act”).⁸ Indeed, the SEC recently has placed greater emphasis on bringing rigorous economic analysis to bear in its own work.⁹ The SEC’s comments in the Order represent another welcome sign of the Commission’s heightened sensitivity to the economic underpinnings of regulatory actions.¹⁰ Given the SEC’s recognition of the value that rigorous economic analysis provides to its own rulemaking process, it is only fitting that the SEC likewise demand greater attention to economic analysis in the context of SRO rulemaking. That is especially true where, as here, the applicable statutory standards and related regulatory requirements encompass economic concepts and considerations.¹¹ ICI recognizes that the NYSE likely faced certain practical challenges in gathering information. We also believe that Broadridge deserves credit for providing information and analysis to assist the PFAC. But, as the Order repeatedly indicates, additional cost and other information—provided or reviewed by an objective third party—is needed to evaluate the appropriateness of proxy distribution

⁸ See, e.g., Sections 6(b)(4), 6(b)(5), and 6(b)(8) of the Exchange Act; see also Rules 14b-1 and 14b-2 under the Exchange Act. ⁹ See, e.g., SEC Press Release, SEC Renames Division

Focusing on Economic and Risk Analysis (June 6, 2013), available at <http://www.sec.gov/news/press/2013/2013-104.htm> (quoting SEC Chair Mary Jo White's statement that "[t]he division serves a central role in the SEC's ongoing commitment to rigorous economic analysis." (Emphasis added.)). See also SEC Staff Memorandum: Current Guidance on Economic Analysis in SEC Rulemakings (March 16, 2012), available at http://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf; Money Market Fund Reform; Amendments to Form PF, SEC Release No. IC-30551 (June 5, 2013), available at <http://www.sec.gov/rules/proposed/2013/33-9408.pdf> (proposing changes to the rules governing money market funds and containing extensive economic analysis).¹⁰ For example, in discussing the proposed basic processing fee and supplemental fee, the Order points out that "[t]he Exchange . . . has not clearly explained why the particular five tiers were chosen, or provided the rationale for the specific differential charges for those tiers. It also offers no evidence that either the Exchange or the PFAC conducted a meaningful review of the economies of scale present in the proxy processing business, or the overall costs associated therewith." 78 Fed. Reg. at 32522. ¹¹ For example, as indicated in the Order, Section 6(b)(4) of the Exchange Act requires that exchange rules "provide for the equitable allocation of reasonable dues, fees, and other charges among its members and issuers and other persons using its facilities." Section 6(b)(5) requires that exchange rules be designed, among other things, to "promote just and equitable principles of trade" and "to remove impediments to and perfect the mechanism of a free and open market" and, conversely, not be designed "to permit unfair discrimination between customers, issuers, brokers, or dealers" Section 6(b)(8) provides that exchange rules must not "impose any burden on competition not necessary or appropriate in furtherance of the purposes" of the Exchange Act. In addition, Rules 14b-1 and 14b-2 under the Exchange Act condition the obligations of broker-dealers and banks to distribute proxy materials to beneficial owners that hold securities in street name on the receipt of assurances from the issuer that it will reimburse the broker-dealer's or bank's "reasonable" expenses, whether direct or indirect. See *id.* at 32521 and n. 267. Ms. Elizabeth M. Murphy June 20, 2013 Page 4 fees.¹² Consequently, we agree that in its current form, the Proposal does not provide the SEC with a sufficient basis to conclude that the bulk of the changes the Proposal recommends are consistent with applicable statutory standards.¹³ Instead, the SEC's comments on the shortcomings of the Proposal—which are very consistent with the concerns we raised in our earlier comment letter¹⁴—underscore the continuing need for an independent review of the proxy distribution system that includes, among other things, a thorough analysis of actual costs involved. We therefore recommend that the SEC disapprove most of the Proposal¹⁵ and that an appropriate third party be engaged to review not only the changes the NYSE has proposed but also the existing proxy distribution fee system.¹⁶ Any such review should include specific analysis of the proxy distribution fees paid by funds and how the proposed changes would affect those fees.¹⁷ ¹² See *id.* at 32524 (stating that ". . . significant questions remain as to the rigor of the Exchange's analysis absent more meaningful cost data and a detailed explanation for the specific levels and structure of the fees proposed, and in light of the extensive reliance by the PFAC and the Exchange on information and recommendations provided by the dominant proxy processor."). ¹³ See, e.g., *id.* at 32523 (indicating that ". . . neither the Exchange nor the PFAC have [sic] articulated a sufficient analysis of Broadridge's costs of providing proxy processing services . . . or of the costs incurred by broker-dealers that may go beyond the services provided by Broadridge. Accordingly, the Commission lacks a sufficient basis upon which to assess whether the incremental changes proposed to the existing fee structure . . . are consistent with the statutory standard, including whether the overall level and structure of the fees reflected in the Exchange's rules are 'reasonable' or an 'equitable' allocation of fees."). ¹⁴ For example, in addition to questioning the rigor of the NYSE's analysis in

general, the Order specifically highlights several lingering concerns with “rebates” (described in the Proposal as “cost recovery payments”). See id. (stating that “[t]he Exchange does not clearly explain . . . why these savings are not passed on to issuers (i.e., why the maximum rates permitted under the Exchange’s rules continue to be charged to issuers in these cases, despite the lower costs incurred)).” The Order further indicates that the payment of rebates raises questions about whether the Proposal meets the statutory standards. See id. at 32523-24. 15 The Commission should approve the proposal to prohibit the imposition of per-name charges for names eliminated in permitted stratifications when an issuer requests a list of non-objecting beneficial owners, or “NOBOs.” Consistent with the recommendation made by several other commenters, ICI supports allowing issuers to request stratification of NOBO lists outside of a record date. See id. at 32520. As we have previously indicated, we are generally supportive of efforts that would make it easier for issuers to use the shareholder communications rules to identify the beneficial owners of their shares and to communicate directly with those beneficial owners. Likewise, we support efforts that would facilitate issuer communications with shareholders throughout the year at a lower cost. See Letter from Karrie McMillan, General Counsel, Investment Company Institute, to Ms. Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, dated April 30, 2013 (commenting on NYSE Euronext Petition for Rulemaking Under Section 13(f) of the Securities Exchange Act of 1934), available at <http://www.sec.gov/comments/4-659/4659-12.pdf>. 16 As the SEC is aware, the Proposal does not address all fees charged in connection with proxy distribution. 17 We note that our earlier comment letter included some data based on a preliminary analysis by an independent proxy service firm of how the proposed fee changes would affect open-end fund special meetings. The NYSE’s response to the comment letters dismissed this analysis, pointing to (among other things) a misunderstanding of what constitutes a “special Ms. Elizabeth M. Murphy June 20, 2013 Page 5 ***** ICI appreciates the SEC’s attention to our comments. If you have any questions, please contact the undersigned at 202/218-3563, or Frances Stadler at 202/326-5822. Sincerely, /s/ Dorothy M. Donohue Deputy General Counsel – Securities Regulation cc: Norm Champ, Director Diane Blizzard, Associate Director Douglas Scheidt, Associate Director and Chief Counsel Division of Investment Management Craig M. Lewis, Director and Chief Economist Division of Economic and Risk Analysis meeting.” See Order, 78 Fed. Reg. at 32521 and n. 260. The response did not change (or specifically address) our view that there is a need for additional analysis of the proxy distribution fees paid by funds.