DIVISION OF
MARKET REGULATION

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

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April 2, 1985

Mr. James E. Buck
Secretary
New York Stock Exchange, Inc.
11 Wall Street
New York, NY 10005

Dear Mr. Buck:

Enclosed is a copy of Securities Exchange Act Release No. 21900 by which the Commission approved your proposed rule change submitted on January 21, 1985 (File No. SR-NYSE-85-2).

Sincerely,

Thomas C. Etter, Jr.
Attorney
Branch of Exchange Regulation

Enclosure

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-21900 ; SR-NYSE-85-2)

Self-Regulatory Organizations; New York Stock Exchange, Inc.; Order Approving Proposed Rule Change

March 28 , 1985

The New York Stock Exchange, Inc. ("NYSE") submitted on January 21, 1985, copies of a proposed rule change pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act") and Rule 19b-4 thereunder to amend NYSE Rule 451 (Proxies), Supplementary Material .91, and NYSE Rule 465 (Company Reports to Stockholders), Supplementary Material .21, to establish a surcharge that may be charged by NYSE members and member organizations to issuers in connection with proxy solicitations. The purpose of the surcharge is to permit the recoupment of start-up costs incurred by NYSE members and member organizations in complying with Rules 14b-1(c) and 17a-3(a)(9)(ii) under the Act, which were designed to facilitate direct communications by issuers to non-objecting beneficial stockholders. 1/

1/ Notice of the proposed rule change together with the terms of substance of the proposed rule change was given by issuance of a Commission release (Securities Exchange Act Release No. 21702, February 1, 1985) and by publication in the Federal Register (50 FR 5461, February 8, 1985). All written statements filed with the Commission and all written communications between the Commission and any person relating to the proposed rule change were considered and (with the exception of those statements or communications which may be withheld from the public in accordance with the provisions of 5 U.S.C. § 552) were made available to the public at the Commission's Public Reference Room.

I. Background

In July, 1983, the Commission adopted new paragraph (c) of Rule 14b-1 under the Act to improve the process whereby issuers communicate with shareholders whose securities are held in street name. 2/ New paragraph (c) requires brokers to provide issuers, upon request and assurance of reimbursement of reasonable expenses (direct and indirect), with the names, addresses and securities positions of customers who are beneficial owners of the issuers' securities and who have not objected to such disclosure. The Commission also adopted a corresponding amendment to Rule 17a-3(a)(9) under the Act to require that the customer records maintained by brokers for street name holders include whether the beneficial owner has objected to the disclosure to issuers of his or her identity, address, and securities positions. To provide time for the determination of reasonable costs by self-regulatory organizations ("SROs") and to minimize costs, the Commission established January 1, 1985, as the effective date for both provisions. Thereafter, associations representing the entities most directly affected by the rules jointly recommended that the effective date be deferred to January 1, 1986, and agreed to facilitate the determination and allocation of reasonable costs and the development of an efficient means of furnishing

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2/ Securities Exchange Act Release No. 20021 (July 28, 1983), 48 FR 35082.

beneficial owner information to issuers. 3/ The Commission deferred the effective date, as requested, in the belief that a cooperative effort would result in the best system for communicating with shareholders while maintaining the system of nominee registration. 4/

In adopting the direct shareholder communications rules the Commission left the determination of reasonable costs to the SROs, because, as representatives of both issuers and brokers, they were deemed to be in the best position to make a fair allocation of the costs associated with the amendments, including start-up and overhead costs. 5/ Accordingly, the NYSE formed an Ad Hoc Committee on Identification of Beneficial Owners ("Ad Hoc Committee"), composed of issuers, broker-dealers, banks, transfer agents, and proxy solicitors, to provide guidance on this issue.

Based on the recommendations of the Ad Hoc Committee, the NYSE's proposed rule change originally provided that the start-up costs associated with the implementation of the rules be funded by a surcharge of $.20 per proxy for each of

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3/ The terms of the agreement are detailed in letters from the Securities Industry Association ("SIA") to the American Society of Corporate Secretaries ("ASCS") and the National Investor Relations Institute ("NIRI"), dated August 3, 1984, from the ASCS to SIA, dated August 10, 1984, and from NIRI to the SIA, dated August 20, 1984. The letters are part of File No. S7-954.

4/ Securities Exchange Act Release No. 21339 (September 21, 1984) 49 FR 38096.

5/ Securities Exchange Act Release No. 20021 (July 28, 1983), 48 FR 35082.

an issuer's two annual meeting proxy solicitations subsequent to the approval of the surcharge. 6/ At the request of the Commission staff, the NYSE has modified its original proposal to apply the surcharge for only one year and has agreed to submit more cost data when it proposes an additional surcharge for the next year's proxy dissemination. 7/ Based on the number of proxies processed in the 1984 proxy season, the Ad Hoc Committee believes that the surcharge, if collected by all broker-dealers for one year will raise $12,500,000 for the securities industry as a whole. The proposed rule change is not designed to assure that, even with a second-year surcharge, each individual broker will exactly recover its

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6/ The cost estimates which served as the basis for the proposal were based on the assumption that broker-dealers would be required to solicit "some 34 million shareowners" as to whether they would object to disclosure of their names and other information to issuers, at an estimated cost of $.70 per shareholder. The 34 million number was taken from a 1983 NYSE survey of all shareowners including those who hold in their own names and those who hold securities through banks. Because broker-dealers only will be required to solicit consent of those shareowners whose securities are held by their broker in street name, this number appears to be inflated. 1983 FOCUS data for all broker-dealers and 1984 FOCUS data for NYSE firms indicates that broker-dealer customer accounts totaled just under 20 million as of December 31, 1984. Therefore, the Commission believes that further cost data is necessary to approve a second year surcharge.

7/ See letter from James E. Buck, Secretary, NYSE to Michael Cavalier, Branch Chief, Division of Market Regulation, SEC, dated March 14, 1985.

start-up costs which are estimated to average $.70 per account. 8/

Both the SIA Operations Committee and the Securities Industry Committee of the ASCS have submitted letters to the NYSE endorsing the proposed rule change. One comment letter, relating to the proposed rule change, filed by Duquesne Light Company ("Duquesne"), was received during the Commission's comment period. 9/ Duquesne claimed that the plain language of Rule 14b-1(c) "evidences an intent that those issuers who request this service bear the costs." Duquesne suggested that a surcharge be assessed only on those issuers who request or indicate they will request the information and that an "appropriate" fee be developed for issuers who request the information at some later date.

The NYSE asserts that insufficient information was available on which to base an allocation of the start-up costs of the number of issuers who would request the data. Furthermore, the Ad Hoc Committee reasoned that an across-the-board surcharge would be the fairest way to recoup

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8/ By far the greatest portion of these costs is attributable to the postage expenses of soliciting account holders as to whether the beneficial owners would object to having their name, address, and security position passed on to the issuer. The balance of the costs is related to systems modifications to collect and maintain this information as required by Rule 17a-3(a)(9)(ii). The SIA cost estimate is set forth in SIA's letter to John S.R. Shad, Chairman, SEC, dated June 25, 1984.

9/ See letter from Diane S. Eismont, Corporate Secretary, Duquesne Light Company, to Secretary, SEC, dated February 22, 1985.

broker-dealer start-up costs. The NYSE stated in its filing that all issuers should share proportionately in the new system's start-up costs because all issuers "might reasonably be expected to benefit sooner or later."

II. Discussion

Under Section 19(b) of the Act, the standard for approval of a proposed SRO rule change is that the proposal be consistent with the requirements of the Act and the rules and regulations thereunder applicable to such organization. Section 6(b) of the Act sets forth the general requirements for exchange rules. Section 6(b)(4) 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 the facilities of an exchange. Section 6(b)(5) requires that exchange rules promote just and equitable principles of trade and that they are not designed to permit unfair discrimination between issuers, brokers, or dealers. Section 6(b)(8) prohibits any exchange rule from imposing any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. In this case, the Commission believes that, to the extent the surcharge is reasonable and fairly allocated, it will meet the standards of the Act.

In determining to have the SROs develop a reasonable allocation of costs, the Commission recognized the need to balance the interests of broker-dealers and issuers in an area requiring difficult estimates. With the exception of the number of account holders, 10/ the estimates which form the basis for the NYSE proposal do not appear unreasonable. Moreover, the fees do not appear to unfairly discriminate among issuers because all issuers have the opportunity to request information regarding their beneficial owners, and more than a narrow class of issuers appears to be interested in receiving this information. 11/ In response to the proposal of Rule 14b-1(c), 152 issuers supported the proposal. 12/

10/ See note 6, *supra*. Even with a reduction of estimated account holders to 20 million, the estimated costs to broker-dealers would total approximately $16 million, substantially in excess of $12 million estimate of the revenue, which will be raised by the first year proxy surcharge.

11/ It is, of course, possible for a rule nominally to apply across-the-board but, by virtue of an uneven impact, to impose inappropriate competitive burdens. The Commission has been unable to identify, and commentators have not asserted, any such impacts from this proposed rule. The costs of this proposal for any given issuer will not be significant, and they will be borne proportionally by each issuer in accordance with the number of proxies it distributes. It could be argued, as alluded to in Duquesne's comment, that it is unfair to impose start-up costs on issuers who have no intention of requesting information on beneficial shareholders. It is unlikely, however, that any such costs will impose a material competitive burden on such issuers. In any event, the Commission believes any such burden is substantially outweighed by the administrative advantages of an across-the-board rule. Accordingly, the Commission finds the NYSE proposal to be consistent with Section 6(b)(8) of the Act.

12/ In a joint ACIS/NYSE survey 643 representative NYSE-listed companies indicated that 55% of the companies wanted the data on non-objecting beneficial shareholders, 18% did not want the data, and 27% did not know whether they wanted the data. Of the 184 companies not NYSE listed who responded (for which there was insufficient data to determine whether they were representative) 62% indicated they wanted data, 18% indicated they did not want the data, and 20% did not know whether they wanted the data.

Furthermore, the Commission believes the proposal is the result of good faith negotiation between representatives of broker-dealers and issuers and is endorsed by associations representing both groups. Accordingly, the amount of the surcharge and first-year payments to broker-dealers appears to be reasonable and thus consistent with the Section 6(b)(4) of the Act.

With respect to the arguments raised by Duquesne, it may be correct that the Commission, in adopting Rule 14b-1(c), anticipated that the SROs would devise a system of fees applicable only to issuers who requested information on beneficial shareholders. Duquesne is incorrect, however, in its suggestion that the Commission mandated such a result or that the language of Rule 14b-1 requires such a result. Rather, in adopting the Rule, the Commission concluded that the SROs were in the best position to make a fair allocation of all the costs associated with the Rule, including start-up costs. Accordingly, the Commission did not limit the SROs' discretion to fashion a reasonable solution. Moreover, the text of Rule 14b-1(c) compels no particular approach to recouping broker-dealer start-up costs. 13/

The statutory standards applicable to SRO rules are written in terms of purposes to be achieved. The purpose of

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13/ Rule 14b-1(c) states in relevant part --

> A broker . . . shall . . . [p]rovide the issuer, upon its request and assurance that it will reimburse the broker's reasonable expenses (direct and indirect), with the names, ...

the proposed surcharge is to establish a fair rate to recoup the costs of a communication system which the Commission determined should be developed. Furthermore, the Ad Hoc Committee determined that user-only funding was impractical because the assumptions required were arbitrary 14/ and presented a substantial possibility that broker-dealers would not be compensated for their legitimate start-up costs, at least not on a timely basis. Accordingly, the Ad Hoc Committee determined that the initial costs of the system to be developed in 1985 should be borne by all issuers, who will then be free to assess whether the incremental cost of actually requesting data on non-objecting beneficial shareholders are off-set by benefits of direct communication with them.

III. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable

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14/ In this regard, Duquesne apparently recognized, but did not address, the complex estimation and cost allocation questions raised by its suggestion that only those issuers who actually request, or indicate they will request, the information be assessed. Faced with the uncertainties and other difficulties posed by such an approach, including the question of how broker-dealers should finance any revenue shortfalls should the number of requesting issuers fall short of expectations, the Commission believes the NYSE, in consultation with groups representing issuers and broker-dealers, reasonably concluded that it was simpler and in the end probably fairer, for start-up costs to be assessed on all issuers who could take advantage of Rule 14b-1(c), not merely those electing to do so.

to a national securities exchange and, in particular, the requirements of Sections 6(b)(4), 6(b)(5), and 6(b)(8), and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the above-mentioned proposed rule change be, and hereby is, approved. 15/

By the Commission.

John Wheeler

John Wheeler
Secretary

15/ The Commission approves the proposed rule change as amended by the NYSE to provide a surcharge only for one year. *See* text accompanying note 7, *supra*.