

# ADVISORY

## SULLIVAN & WORCESTER LLP CORPORATE ADVISORY

### Elimination of Broker Discretionary Voting in Director Elections

The Securities and Exchange Commission has approved amendments to New York Stock Exchange Rule 452 that eliminate broker discretionary voting in uncontested director elections. The amendments will be effective for shareholder meetings held on or after January 1, 2010. Because many brokers are members of NYSE and subject to its rules, these changes impact not only NYSE-listed companies, but companies listed on NASDAQ and other national securities exchanges.

#### ***What is Rule 452 and What Will Change?***

Under NYSE rules, brokers holding a company's shares in street name are required to transmit the company's proxy materials to the beneficial owner of such shares and request the beneficial owner's voting instructions. If a broker does not receive voting instructions from the beneficial owner ten days before the date of the shareholder meeting, the broker may nevertheless vote those shares on matters considered by NYSE to be "routine", but not on matters considered to be "non-routine".

Prior to the amendments to Rule 452, uncontested director elections were considered routine; therefore, brokers could exercise their discretion in voting on such elections if no instructions were received. The amendments to Rule 452 expand the definition of non-routine matters to include all director elections, whether contested or uncontested, except for companies registered under the Investment Company Act of 1940. After the effective date of the amendments, brokers will not have the right to exercise discretionary votes in any director election, except for investment company directors.

#### ***What Are The Implications Of This Amendment?***

The amendments will have a number of practical implications for companies:

- **Quorum.** As a result of these amendments, companies may have difficulty achieving quorums for conducting business at shareholder meetings. Discretionary votes of brokers often constitute a significant portion of the shares represented at a shareholders meeting, and are therefore important in

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establishing a quorum. Including another routine matter (such as the ratification of the appointment of a company's independent auditor) for which brokers may cast discretionary votes could help companies establish a quorum since, in most cases, a quorum on any item establishes a quorum for the whole meeting.

- Majority Voting. For companies that have adopted a majority voting standard with respect to the election of directors, the directors must obtain the vote of a majority of the votes cast in order to be elected. Historically, brokers have exercised their discretion in uncontested elections by voting for the directors recommended by the board. Without broker discretionary votes in uncontested elections, it may be more difficult for each director to obtain a majority affirmative vote.
- Institutional Investors and "Just Vote No" Campaigns. The amendments are likely to increase the influence of larger, institutional shareholders as they are historically more likely to vote than retail shareholders. The elimination of broker discretionary voting will, therefore, likely disproportionately reduce the votes of retail shareholders. In addition, "just vote no" campaigns are likely to be more successful in the absence of broker discretionary voting. Because brokers generally vote for the board-recommended directors, there could be fewer votes in favor of each director. Therefore, it may be easier to solicit enough "against" or "withheld" votes to outweigh the votes "for" a director, particularly for companies with majority voting.
- Notice and Access (E-proxy). The elimination of broker discretionary voting may discourage companies from taking advantage of the new e-proxy rules. Companies using e-proxy have experienced a decline in the number of shareholders voting as compared to the more expensive traditional, hard copy full set delivery method. The decline in voting is particularly pronounced with respect to retail

shareholders. Companies may determine that, with the elimination of broker discretionary voting, it is necessary to use the traditional delivery method in order to secure the maximum number of votes, particularly for companies who have a large portion of retail shareholders.

- Expenses. Due to the issues discussed above, companies are likely to incur additional costs in connection with shareholder meetings and director elections, such as engaging proxy solicitors, to ensure that the requisite votes are obtained.

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The summary above is intended to give a broad overview of the amendments to NYSE Rule 452 and the implications of such amendments. For a more comprehensive analysis of these changes, or for further information about the impact of these and other recent SEC changes, please contact the lawyer at Sullivan & Worcester LLP with whom you regularly consult, or the lawyers listed above.