WHAT’S RELEVANT?
A Quarterly Update of AST’s Executive Advisory Council

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EAC Proxy Lookback

YEAR-END PROXY RECAP

D.F. King & Co., Inc. (“D.F. King”) recently published a 2018 Year-End Proxy Recap Guide, which serves to provide issuers with a review of key trends for 2018 as well as insights into the 2019 proxy season to help guide engagements with investors. Below you will find a summary of a few key findings detailed in the guide as they relate to shareholder proposals, board diversity and executive compensation. For a full copy of the guide, please click here.

Shareholder Initiatives

The Debrief

- Environmental & social proposals continue to be a main focus for investors, with submissions for both general categories together totaling almost half of all shareholder proposal submissions. Environmental & social support continues to gain traction in 2018, with numerous proposals receiving above 30% votes cast.
- As for proposal submissions, social issues have taken the lead in 2018. Increased investor efforts include campaigns for lobbying and political contribution disclosures, board diversity, social reporting and gender pay gap disclosures. Environmental proposals also continued to have a strong presence.
- For governance proposals, 2018 was the year of the special meeting proposal. This type of proposal constituted the largest subcategory of governance-related proposals for 2018.
- New types of shareholder proposals for 2018 have followed popular headlines, and include proposals on gun safety and violence, as well as proposals on content management and ‘fake news’ at social media companies.
- Success rates for no-action requests have dropped by approximately 12%, increasing the importance of engagement.

Board Diversity

The Debrief

- Disclosure regarding board refreshment and diversity has become far more prevalent. Skills matrices and discussions regarding the director recruitment process have an increased presence in proxy statements filed in 2018, as a direct response to pressure from investors who are looking for increasingly diverse boards and information on what processes companies have in place to achieve this.
- Many companies this year have strengthened their commitments to increase board diversity to negotiate the withdrawal of these shareholder proposals, as well as to overturn negatives votes against directors cast by institutional investors regarding this issue.
- Gender diversity on boards continues to increase. As of 2018, 47% of the S&P 500 has at least three women on the board. 38% of the Russell 3000 has at least two female directors. The percentage of newly elected directors this year who are female constitute approximately 35% of newly elected directors in the Russell 3000.
- Large institutional investors are increasingly voicing their support for board diversity. For example, BlackRock amended their
voting guidelines earlier this year to express their belief that companies should have at least two women on the board. Other asset managers such as State Street and the NY State Retirement Fund have indicated that they will vote against boards without any female directors.

• The NYC Funds’ ‘Boardroom Accountability Project 2.0’ is focused on board diversity disclosure, with an emphasis on skillsets. This year, 151 companies received a letter from NYC Funds Comptroller Scott Stringer asking for increased board skill disclosure in the form of a “skills matrix”.

Executive Compensation
The Debrief

• Although Say-on-Pay failures have increased, average support remains high at approximately 90%. 2018 was marked by a handful of high-profile Say-on-Pay failures that gained significant media attention.

• Equity plans remain uneventful, with fewer failures and a continued high level of support. Many of the revisions to plans placed on the ballot this year were due to the fact that Section 162(m) of the tax code was eliminated.

• Shareholder proposals regarding executive compensation have increased, with proposals requesting to tie environmental & social proposals to executive compensation taking the lead.

LEARN MORE
For more information regarding the services offered by D.F. King, contact Zally Ahmadi, D.F. King’s director of Corporate Governance & Executive Compensation, at zahmadi@dfking.com.
Unclaimed property audits have been part of our landscape forever. Years ago states would target companies that had gone through a merger, or companies that did not report their general ledger (payroll, payables, etc.) in order to review their securities books and records. Over time this practice has increased and states are now extremely active in the audit arena.

Kelmar Associates, a contingency fee based audit firm, was originally contracted by 18 states in 2017 to perform audits, not just on individual issuers, but the transfer agents books and records. This provides access to the shareholder records for all shareholders in the affected states (now up to 22) and the issuers that may be incorporated in those states. This has lead issuers to ask many questions.

While there is no exact time frame for these audits, most audits go on for over a year. “Securities only” audits may conclude within 2 years, but the new exams are taking a longer period of time. It is very common for Kelmar audits to take 2-5 years. If the issuer and/or Transfer Agent is producing information quickly, and Kelmar isn't turning it around at the same pace, the holder can go directly to the states and insist that Kelmar focus on the holder and get the audit done. However, frequently the duration is due to the high volume of demands from Kelmar. There is not much the holder can do in this situation.

Kelmar continues to solicit states for audit, adding four states in the past six months. We have also seen the introduction of other

### HOW WE GOT HERE

1. **Rise of the 3rd Party Auditor**
2. **Auditor interpretations vs. actual law**
3. **GL to securities progression (and back again)**
4. **The Delaware Initiative**
5. **Audit scope expansion**
6. **State benefits**
audit firms being engaged by states over the past year. States engage auditing firms due to most of them not having the resources, budget, or securities expertise to conduct audits themselves with state employees. The audits focus on property that Kelmar believes may be late. Quite often the property identified is not late in accordance with state statutes, rather it’s late according to Kelmar’s interpretation of the state statute.

In order to defend these audits, it is imperative that issuers work closely with their transfer agent. Transfer agents can offer guidance and expertise on the facts and the process, as well as introduce the issuer to various asset recovery programs that may mitigate the amount of unclaimed property on their books. Issuers may also look to hire an advocate. The advocate is the expert on the law and whether the audit protocol is within the boundaries of the law. It is usually very effective for an advocate and Transfer Agent to work together on behalf of a client, providing the advocate understands securities law.

Once the audit is completed, Kelmar will issue a Report of Exam (“ROE”). If the holder agrees with the ROE, the state will make a demand for the property deemed unclaimed. At that time, the holder will negotiate closing agreements/releases with each state and arrange for the demand to be met, and the securities and cash are transferred to the state.
Understanding human behavior is the first step in developing best practices for excellent shareholder interactions

AST’s on-going industry studies to examine shareholder interactions and its programs to ensure shareholder satisfaction and education have created services benchmarks and best practices for the ideal shareholder interaction. Through these AST initiatives, the researchers and AST executives have learned that gaining an understanding of human nature is the first step in the development of best practices for shareholder interactions.

Consider these shareholder comments that illustrate situations where shareholder rights and mandated actions can run counter to everyday human behavior.

“I didn’t realize that the state would take my shares. I’ve been travelling. Why didn’t someone tell me about this?” This comment came from a shareholder who had been contacted several times over many months, electronically, by phone and even by mail using multiple addresses. He just never imagined that his shares could be removed without his permission but did not take time to read the ramifications described in the material sent to him.

“Why can’t you mail me a Statement? I hate going online” This missive came from a shareholder who agreed to go paperless just a few weeks earlier.

“My uncle gave me these shares, why do I have to go to so much trouble to have them put into my name.” The heir apparent here was uninformed that corporations are required to validate the new owner’s identity and that this could not happen automatically.

Both corporations and services providers have heard these comments and more describing situations that can be avoided or at least minimized with best practices for shareholder interaction that are based on an understanding of human nature.

Here is a sample of these Best Practices Guidelines that AST has explored and has taken action to implement. These ideas always keep in mind that the shareholder is a precious asset and deserves service that is in keeping with this important ownership role.

Shareholders have limited knowledge of financial terminology and need help in understanding it, even the simplest ideas among the most knowledgeable shareholders.

Best Practice: Explain everything and in more than one place.

In a recent AST study, it was found that the term “escheatment” had low levels of awareness and understanding, even among highly educated shareholders. Common financial terminology held limited interest and understanding as well. However,
corporations and services providers may come to believe that their everyday terminology (or you might say jargon) is known to everyone. To be fair, shareholders may only use this terminology at various inflection points in their financial history. To remedy this lack-of-easy understanding, it is recommended that communications be tested for understandability, preferably amongst an audience not currently working at a financial institution.

By changing this attitude and critically assessing language used, communications are much more successfully received. Additionally, including a well-crafted Frequently Asked Questions allows the shareholder to educate themselves without feeling intimidated or foolish.

AST research shows that shareholders want to be communicated to on multiple channels. For example, if a shareholder action is required because of a merger or acquisition, shareholders want to be able to get a print copy of a required form as well as be able to access it online should they need another copy. Sometimes having materials both in print and online improves the shareholders belief that what they have received is credible and important.

Humans have a very limited sense of time, often underestimating or overestimating time available for an activity.

Best Practice: Always be as specific with dates, deadlines and approximate time to complete the work.

Social science researcher and Nobel Prize winning author Dr. Daniel Kahneman discussed in his book, Thinking Fast & Slow, that the human brain has two modes of action.1 When it comes to time, we are programmed to take fast action if we sense a danger and that is one aspect. On the other hand, for things that require consideration of future events, we are likely to set this mode of action aside and work more slowly so we have more time to study the matter carefully.

AST research on shareholder materials has supported this understanding. If a mailing is large with many attachments, the shareholder is likely to set that material aside to look at it at more convenient time. On the other hand, materials that had optimum materials and included a specific time for response, shareholders reported they were more likely to respond immediately in order to make the deadline comfortably.

The corporation and the services provider is in a difficult position because most shareholder interactions are time sensitive and are relatively complex, at least to them. If communications require quick action but are presented in a complex way, chances are good the shareholder will set the communication aside for review at a later date, often inadvertently going beyond the deadline, creating extra costs and the perception of poor service.

AST research has shown that relative terms such as “reply immediately” are not well-received and often misunderstood. For an activity such as a merger or acquisition buy back, communications need to be completed by a specific date. If the communication is complex, the term “immediate” may be translated to mean, “When I get time to study it.” Additionally, if the shareholder is given too much time, the activity falls into the cracks. If they do not get enough time, shareholders can have a negative experience. Three weeks is considered a good timeframe for notification; however, testing can help to identify optimum delivery and action points for various activities.

Shareholders participating in AST research have also indicated that knowing the approximate time to complete required work helps improve their satisfaction with the interaction. By setting expectations, corporations and providers can minimize

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thoughts such as “I didn’t realize it would take this long.” These shareholders asked for honesty in predicted time to complete so they could plan accordingly.

When paper forms are mailed, it is also helpful to let the shareholder know that mail can take longer. Providing options for scanned documents so reply is immediate is also viewed as helpful, particularly by shareholders who are comfortable with computers and internet usage.

Human personalities come in a variety of forms and characteristics. What works for one shareholder may be a deal breaker for another.

Best Practice: Study your shareholders and profile their behavior directing them to messages and channel of communication that will provide the best experience for each of them.

The AST shareholder research demonstrate that different shareholders demand different manner of interaction. While regulations require that all shareholders have equal access to information, styles of communicating can influence a shareholder’s satisfaction. Some people may be uncomfortable with online access and prefer print formats. Others may agree to an online format and then fail to visit the online information potentially missing important communications and account updates. Often these shareholder differences can be attributed to lifestyle, psycho-demographic profile, life stage or workstyle, among other ways of categorizing shareholders.

An important first step in better experiences for shareholders is to better define and understand them. A discovery and analysis of shareholder demographics may be of great help in building the right tools. For example, if the 50% or more of your shareholders are over 65 years of age, you may want to look closely into what the impacts are when you seek to stop mailing statements and go totally to online accounts. The company would need to assess the costs of these shareholders having difficulty. Will these older shareholders ratchet up their calls to you or your service providers or decide to sell the stock or be otherwise unhappy?

A good example that AST has found effective is to offer shareholders different channels of communications. If an older shareholder base is having difficulty with self-service, AST offers online chat help or directs the shareholder at least temporarily to telephone assistance, among other strategies to support the shareholder and the corporation.

There are ways to segment shareholders into clusters or categories that will enable better support of each cluster-type. Through the use of advanced statistical analysis and Voice of the Shareholder research, corporations and their services providers can develop these useful models and operational rubrics.

Implementing change, even a positive change, can challenge shareholders.

Best practice: Frame changes as evolutionary and demonstrate ease of use as well as the benefits of the change.

Researchers around the world have seen that when a change is made, people are uncomfortable with that change. It simply takes more brain power until the shareholder is accustomed to the new situation or method. It will take time to learn the new way, even for simple changes. Everyone can identify with upgrades in software that offers many benefits if only we can figure them out.

Researchers and decision theorists have found that people will prefer something they know over something they do not know, even if the odds for success are better with the concept that is new to them. The best practice, of course, is not to stop innovating and changing but rather innovate and change while constantly reminding the shareholder of the connection to the familiar, the ease of use and offer plenty of help while the shareholder
educates himself on the new and ultimately better way to handle tasks. Education, support while changing and practice makes it easier to overcoming this human nature bias.

When developing a new system or practice, offering education and a little help will be paramount to the shareholder. Easily available help, even for things that appear totally user-friendly to the developer need explanation and just that little crutch that will make the shareholder comfortable.

Researchers have also found that a little humor and fun make education and learning new systems and methods much easier. While services providers are dealing with serious subjects, a smile in the voice of the representative makes a world of difference. AST training for its service representatives, executives and its evaluation programs provides needed practice and guidance to provide the best possible service response.

**Forming habits takes time. When new systems are developed, it takes time for the use to become easy and part of routine or habit.**

**Best Practice: Give shareholders time to react and acclimatize to new systems and procedures. Expect the unexpected. Have patience.**

With shareholder interactions, AST operations has shown that we are faced with several dilemmas around habit. First, some shareholder interactions happen very infrequently and may even be once in a lifetime situations. As a result, habit, which make everyday life easier, does not come into play. In another case, shareholders may be looking at their account status in one way for many years and have formed the habit of signing on in a certain way and so forth.

New habits take time to form. While innovators and developers, hope that new ideas will be recognized immediately, research indicates it takes 30 days or more for a new way of doing things to embed in an individual. Full adoption by a group takes even more time. It has been shown that in the early stages of development, many people actually view the new technology in a poor light and can score the service lower than it will in the future. This is seen even though the new system offers a better solution with added benefits.

AST recognizes and prepares for shareholder confusion or need for help. Training comes into play to help the customer service representatives bring the right tools to the situation. For example, emotional control is paramount no matter what circumstances the shareholder presents. When a shareholder is stressed or experiencing difficulty because he or she is outside his/her comfort zone, it has been found that communicating from a non-emotional-reactive stance builds confidence and trust allowing the new habit to form more readily.

Being ready to be surprised is another cornerstone of best shareholder interaction. Even with the best of planning, a shareholder can amaze us with a new situation or an unexpected twist on an old situation. Remaining confident that an answer can be found or is possible will work like magic to calm an upset shareholder. Being prepared to handle the unexpected is an important best practice. Using words that suggest positive situations and imagery help to bring the shareholder successfully into the discussion.

**Shareholders recollection of an interaction will be based on the peak interaction and the last interaction.**

**Best Practice: Strive for perfection throughout an interaction and never waiver until every aspect is complete and more.**

AST recognizes that shareholders are a company’s most important asset. As such, each interaction is designed to provide the optimum experience for the shareholder.

What research has shown AST is that at every step in an interaction a client can be pleased or dissatisfied. Even if the shareholder
interaction is complete, how the customer service representative wishes the person goodbye will impact how the shareholder evaluates that interaction.

The notion of highs and lows in a shareholder interaction is supported again by author Dr. Daniel Kahneman. His research into clinical interactions helped him theorize on what he calls the “Peak-End Rule.” Simply put, people judge an experience largely based on how they felt at its peak (i.e. its most intense point) and at its end, according to Dr. Kahneman.

In view of this theory and AST’s own research, AST’s best practice involves considering each step of an interaction and how to improve performance not just in the main event or activity of the interaction but at every step with particular attention paid to the final communication with the shareholder.

Sometimes, shareholders must be told news they find unwelcome. All is not lost in these transactions if a positive resolution is found at the end and the shareholder feels confident that he can trust the outcome and knows what will come next. Maintaining positivity with language and confidence, keeps the shareholder engaged and not seeking to unnecessarily escalate the issue to another level. The services provider uses the interaction to make improvements so every shareholder experiences offers an opportunity for continuous improvement.

While it’s impossible to determine what every shareholder will do, making sure the experience is positive will increase the likelihood of satisfaction with the overall interaction. Perception often becomes reality.

**Empathy is your best tool to create positive shareholder experience. Shareholders expect to be treated as a valued investor. People respond to personal communications.**

**Best Practice: Treat Every Shareholder as a Special Individual.**

Benchmarking other industries to discover best practices is another research method AST uses to study shareholders and their clients’ needs. After studying many models, best practices and its own research, an essential finding is that shareholders want to be treated as individuals. They want to trust their business associates. Satisfaction is built on trust that in an interaction corporations and service providers will know them and will be their advocates and champions.

Keeping and believing this philosophy of “Shareholder as respected friend and valued investor is the first and most important step in this best practice.” There are ways to signal this philosophy in everyday practice. Of course keeping the response fresh, genuine and proactive cannot be overstated.

Consider the shareholders name. People like to know you know them as an individual. Addressing shareholders by name in correspondence and in person is an important best practice. In AST research, it was determined that shareholders evaluate the importance of a correspondence by the way they were addressed. While they were understanding that sometimes correspondence had to occasionally be generic, they usually did not review generic correspondence with a serious mind.

While first names are today’s commonplace usage, research indicates that many people prefer to be addressed by their desired prefix and last name. Addressing the person correctly is so important and it changes with the age difference in the individuals or relative seniority. For example, in research programs, the researchers always address Board members or senior executives as Mr. Ms., Mrs., or Dr. and ask permission to use the first name as the engagement continues and where appropriate. For formal correspondence, the full name is used and for informal meetings or conversations, the first name can be used with permission.

A show of friendship or empathy also helps to cement the shareholder relationship. Good nature and a genuine level of understanding helps to smooth over sometimes difficult messages and turn of events such as a State-
forced escheatment or a grief-laden change of ownership.

Shareholders want to know that someone has their backs. Many years of AST research with corporate issuers, have shown that having a shareholder contact the CEO to complain about a situation is a worst-case scenario. Research also tells us how these situations can take place and how to head them off. At the heart of an escalation is the shareholder’s desire to talk to someone with the ability to take care of their problem. One best practice to avoid this upscaling is to make sure the shareholder knows the name and title of the person they are working with.

From the beginning of the interaction, whether in phone, online or print, knowing there is a real person with the technical knowledge to help them or show them where to find the answers fast creates a more positive experience. Shareholders want to know to whom they turn for assistance with a problem they cannot solve themselves.

Shareholders should never feel they have nowhere to turn for help.

To provide the most effective service, determining the shareholders specific goal for the interaction also gets more quickly to the solution. Learning what the shareholder really wants to do lets the shareholder know you understand them and have the skills to advise them. Guiding a shareholder to the right channel of communication and the right solution is a hallmark of good shareholder service.

These are just a few ideas for best practices to successfully work with shareholders. AST continues to research shareholder needs seeking opportunities for continuous improvement. If you have a situation that illustrates a best practice, contact the author or your Relationship Manager at AST or D.F. King & Co., Inc.. We look forward to hearing from you.

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