

Electronic Voting is Finally Gaining Ground

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Empirical data suggests that investors are finally warming up to the idea of electronic voting. Last year, nearly 10% of public stockholders voted electronically.¹ Current estimates suggest that this percentage will increase dramatically over the next several years.² Correspondingly, over the last 2 years, almost half the states have changed their corporation laws to allow electronic voting.³

Introduction

Electronic voting is the practice of enabling stockholders to vote (*i.e.*, approve corporate action requiring stockholder authorization, either through written consent or proxies) in

¹ Neil Hare, *Web-Based Proxy Voting Growing; Provides Shareholders Louder Voice*, CORP. LAW WKLY., Jan. 10, 2000, at 1.

² See, e.g., *Lucent Technologies, Con Edison and Others Offer Online Proxy Voting to Shareholders* (visited 12/1/00) <http://www.shareholder.com>.

³ For example, Delaware law permits a stockholder to authorize a third party to serve as their proxy through any means of electronic transmission. See DEL. CODE ANN. tit. 8 § 212 (2000).

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connection with annual meetings and significant corporate events such as mergers and acquisitions, either by telephone or over the Internet. This practice typically involves issuing a stockholder a proxy statement and proxy card through the mail or over the Internet and establishing a toll-free telephone number or website for stockholders to vote. In conjunction with the proxy statement and proxy card, each stockholder receives a unique identification number for voting purposes. This is designed to ensure that no stockholder votes more than once and to otherwise prevent fraud. And, of course, each method includes basic instructions for stockholders to follow in casting their individual votes.

Although voting electronically may be accomplished through a variety of means, the future of electronic voting rests decisively with the Internet. Nearly 40% of votes this year were cast electronically. This is compared to just 20% by paper and a mere 5% by telephone.⁴ In light of these statistics, it is apparent that investors are enthusiastic about not only trading their stock over the Internet but also about registering their opinions regarding matters of corporate governance over the Internet as well.

Unlike traditional voting where the proxy card is sent by mail to the stockholder, subsequently signed and returned by mail, electronic voting raises a host of additional regulatory concerns ranging from whether stockholders have access to the Internet to whether electronic proxies should also be supplemented with paper proxies. The task of how to confirm the delivery and receipt of electronic proxies also raises a major challenge, since the entire voting process is contingent on the accessibility and reliability of computer systems. The security and confidentiality of electronic votes are also an issue in an age when concern over online privacy has reached its peak.

SEC Guidance on Electronic Communications with Stockholders

The SEC has issued several releases addressing regulatory issues relating to the dissemination of information electronically and electronic voting in particular.⁵ These releases make clear that all proxy rules remain in effect with respect thereto. They also set forth the additional requirements to be met by companies using electronic media for these purposes.

The predominant principle among all the SEC releases which address the electronic dissemination of information is that the information must be delivered in a manner which is *substantially equivalent* to the information delivered in paper format. Therefore, while the SEC

⁴ *Proxy Season Replay: Electronic Voting Wins, Internet Lags Paper and Phone Proxy Solicitation Continues to Fall, While Online Voting Picks Up the Scraps*, INV. REL. BUS., Aug. 14, 2000, at 1.

⁵ *See, e.g.*, Securities Act Release No. 33-7233, (Oct. 6, 1995) (addressing the use of electronic media for delivery purposes); Securities Act Releases No. 33-7288 and No. 33-7289, (May 9, 1996) (discussing the use of electronic media for the delivery of information by broker-dealers, transfer agents and investment advisers); and Securities Act Release No. 33-7856 (Apr. 28, 2000) (clarifying the predominant requirements of the use of electronic media as detailed in earlier SEC releases). *See also* Electronic Signatures in Global and National Commerce Act, 15 U.S.C.A. §§ 7001-7031 (2000) (requiring that consent to receiving information via an electronic medium must be submitted by recipient in a form which ensures their ability to access the relevant information).

has accounted for the mechanical differences involved with electronic dissemination, the actual substance of the information is required to be the same regardless of dissemination format.

Besides the requirement that information delivered electronically must be *substantially equivalent* to that in paper format, the SEC has three additional prerequisites to valid electronic communication with a company's stockholders. The first is that, prior to electronic delivery of information, stockholders must have both *timely and adequate notice* of how and when the information may be accessed. This *notice* element necessarily requires the precise time and date of electronic delivery in addition to where and by what means the materials may be received. In the case of an electronic delivery being made over the company's website, for example, the notice must include the address of the website plus the time and date the materials are to be available.

The *timeliness* element requires notice in *close proximity* to the time that official delivery in paper format would have taken place. In other words, the guiding principle is that electronic communications should be received by stockholders within the time frame required as if the same materials had been delivered by mail. In the case of a Delaware corporation's annual meeting, therefore, an electronic notice must be sent to stockholders no less than 10 days and no more than 60 days before the date of the meeting.

Effective access, another prerequisite to a valid electronic communication, must ensure stockholders' ability to quickly and easily gain access to the information. Quick and easy access to the information must be accompanied by means enabling stockholders to print or otherwise maintain a file copy of the electronic communication. Effective access also requires that stockholders retain the right to receive that same information in paper format.

Finally, there must be proof of the delivery of the information by electronic means. Evidence of delivery may be established in several ways. E-mail return receipts are perhaps the most popular means in certifying the delivery of information electronically. Other ways of establishing proof of delivery include keeping a record of stockholder visits to the relevant website, the return of a special form only available through accessing the website, or obtaining hard copy proxies or written consents which the stockholders printed off a website, signed and returned by mail or facsimile.

Benefits of Electronic Voting

While all electronic communications with stockholders afford substantial benefits, electronic voting may be the most positive trend from the perspective of both companies and their stockholders.

Corporate boards may find electronic voting critically important when time-pressured corporate developments are involved. For instance, by markedly reducing the amount of time associated with the printing and mailing of paper proxies, electronic voting permits full-scale proxy solicitations to be accomplished rapidly.

Approval of a merger, for instance, which ordinarily requires an affirmative vote of a majority of the company's outstanding shares, may be shortened by a week or more since proxy

materials may be made accessible over the Internet, thereby avoiding entirely the cumbersome delays associated with mailing proxy materials and awaiting the return of proxy cards through the mail.

In addition, electronic voting can substantially reduce printing, fulfillment, mailing, tabulation and other costs. These reductions do not come at the expense of stockholders who cast votes by telephone using a toll-free number or cast votes over the Internet, for example, via computer modem or cable or DSL connection which usually involves nominal, if any, cost.⁶

Aside from the benefits like lower costs and reduced response time, electronic voting has been viewed as fostering corporate democracy and stockholder activism since it typically results in increased stockholder response. One recent report even indicated that, when stockholder employees were afforded the opportunity to vote over the Internet, participation rates were considerably higher, reaching levels approaching 50 percent.⁷

Other Requirements

In addition to complying with SEC releases governing the electronic dissemination of information to stockholders, compliance with state law, with a company's articles of incorporation and bylaws, and with the rules of the relevant securities market, such as the NYSE and NASDAQ, are necessary. The NYSE's Rule 452 mandates that proxy statements and annual reports be filed in paper format. On the other hand, the NASD requires its members to comply with the electronic delivery requirements as specified in the SEC releases.⁸

Regarding state law, some states like Delaware expressly allow the electronic transmission of votes. Yet most states, while not prohibiting the electronic dissemination of materials to stockholders, are silent as to its permissibility. Nonetheless, laws permitting digital signatures may be sufficient provided that there is no direct bar to voting with digital signatures. And with the federal Electronic Signatures in Global and National Commerce Act, which became effective on October 1, 2000, there is a substantial likelihood that digital signatures will be the norm since the new law presumptively supersedes most state rules.⁹

Most state laws also require a *written* notice of meetings of stockholders. Unless the state law is construed to mean that a digital proxy statement is such a notice, a waiver of a *written* notice must be executed by stockholders. Accordingly, the company must make arrangements to receive from stockholders their written consents to the electronic delivery of the notices of meetings.

⁶ Ronald H. Gruner, *Electronic voting: The best is yet to come* (American Society of Corporate Secretaries), Summer 1998, at 2.

⁷ Between 50% to 70% of all electronic proxy voters vote within the first 2 weeks of receiving their proxy materials. *See id.*

⁸ *See* 1998 NASD Notice to Members 98-3, *Electronic Delivery Of Information Between Members And Their Customers* (Jan. 1998).

⁹ *See* Electronic Signatures in Global and National Commerce Act, *supra* note 6, § 7004(b)(2)(c)(i) (preempting state law by recognizing validity of digital signatures when recipient has expressly consented, unless there is a *substantial justification* for state law).

Additionally, customary corporate bylaws provide that proxies be either written or signed. Therefore, steps may also need to be taken to appropriately amend the bylaws in making the electronic transmission of proxies commensurate with corporate authority.

Finally, and perhaps most importantly, express disclosure in the proxy materials that electronic voting is available to stockholders is always necessary.

Conclusion

In view of the increasing popularity of the Internet and developments in technology that make electronic media more accessible, most companies can be expected to soon prefer the ease of use and diminished costs associated with the electronic dissemination of corporate information. The proliferation of company websites, webcasts and press releases via e-mail are only a small part of an increasing trend towards electronic media becoming the prevailing mode for corporation communication. Accordingly, companies should continue to adapt to this technological revolution by adopting policies designed to enhancing access to corporate information as well as the ability of stockholders to participate in corporate governance via the Internet.