September 12, 2018

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE Washington, DC 20549-1090
Re: File Number 4-725; SEC Staff Roundtable on the Proxy Process

Dear Mr Fields,

I welcome the opportunity to contribute to the Securities and Exchange Commission's Roundtable on the Proxy Process, which includes a focus on the role proxy advisors play in corporate governance and capital markets – something I have direct experience of.

Hopefully my experience with Institutional Shareholder Services (ISS) will provide the SEC with an insight into the difficulties smaller companies in every jurisdiction face when dealing with the rigid policies and methodologies of proxy advisors. Those policies – developed without any level of transparency – fail to take account of individual company size and circumstance. Through rigid application and superficial oversight from employees, the approach of proxy advisors has the potential to disproportionally impact smaller companies and, as a result, capital markets generally.

Below is a piece I wrote in the Times as a result of my interaction with the world's largest proxy advisor, ISS, subsequent to Elegant Hotels' (a UK listed company of which I am a Board member) AGM in February 2018.

Bungling, box-ticking hypocrites who tried to kick me off a board

It seems I am no longer fit to serve. Or at least that's what an organisation called Institutional Shareholder Services (ISS) has said: it recommended that I should be voted off the board of Elegant Hotels Group.

ISS is almost unknown outside the professional investment community but its influence in the business world is considerable. A private American company controlled by a private equity firm called Genstar Capital, ISS invented the proxy advisory industry 33 years ago. Now thousands of institutional investors outsource analysis of matters such as executive compensation and board diversity, and often take its advice on how to vote their shares.

I assume its clients believe that ISS knows more about corporate governance than almost anybody. It certainly claims to be a thought leader on the subject, boasting that it scrutinises the governance of 40,000 public companies. However, ISS has only 370 professionals, so I don't think its staff can research each business very deeply. For example, their analysis of Elegant Hotels was superficial, and their biography of me was inaccurate.

I have spent more than 25 years serving on the boards of a number of public companies; I wonder how many years of directorships the team running ISS have amassed. Not many, I suspect. It sounds a bit like eunuchs giving sex lessons. I would have thought direct experience was essential for the job.

It is ironic that an American firm is lecturing British plcs on how to run their boards. In my experience, many US public companies suffer from three big defects uncommon in Britain: they frequently have a combined chief executive and chairman; they often have finance directors who are not qualified accountants; and they typically meet only six times a year, or even less. Moreover, many US listed companies have poison pills and non-voting shares, which are almost unheard of in the UK.

A big reason why there are fewer listed companies than there used to be in places such as Britain and the US is the presence of corporate governance zealots. Entrepreneurs prefer to keep their businesses private, away from intrusive box-tickers such as ISS. Wealth creators don’t want bureaucrats lecturing them about who can be on the board, how much directors can be paid, and whether their operation is suitably sustainable. Meanwhile, private equity has been the big winner from all the nannying nonsense, welcoming stock market defectors with open arms. How is reducing the pool of quoted equities helping institutional investors?

In particular, ISS appears to apply its rigid principles to smaller companies such as Elegant, which is on AIM and so does not have to comply with the UK Corporate Governance Code. It is simply not practical or appropriate for the likes of Elegant, capitalised at less than £100m, to adhere to the ISS rule book. It already has endless Companies Act and London Stock Exchange requirements, with auditors and nominated advisers monitoring its accounts and behaviour.

One of the criticisms of me made by ISS was that I was not independent because I am the largest shareholder in the company, but surely it is helpful to have an unpaid non-executive director with more than 25 years’ experience in the hospitality industry, especially when there are millions of pounds at stake?

The one-size-fits-all policy for governance does not work and damages capital markets. Only lazy fund managers and proxy advisers with a vested interest in stirring up trouble can think a single set of rules makes sense.

Unfortunately for the investment community, ISS operates a duopoly with another US private company called Glass Lewis. These gatekeepers are not specifically regulated; in essence, they invent their own rules and act as judge and jury when assessing public company governance. Their dominance enables them to give a stamp of approval to plcs that adhere to their diktats; of course, this doesn’t mean such “certified” companies are well managed or indeed make money for shareholders.

ISS and Genstar are private, so we can’t investigate their finances. Interestingly, though, they don’t tick all the diversity boxes: all 15 ISS bosses are white, while Genstar has only one woman on its 15-strong leadership team, and all its 24 strategic advisers are white males. Perhaps before lecturing others, they should put their own houses in order.

Regards,
Luke Johnson
Risk Capital Partners