



November 9, 2018

Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

**Re: SEC File Number 4-725 on Roundtable on the Proxy Process -
Proxy Advisory Firms**

Dear Mr. Fields:

The Society for Corporate Governance (the “Society”) appreciates the opportunity to provide comments in response to the U.S. Securities and Exchange Commission (“SEC” or “Commission”) on the proxy process and related SEC rules in advance of the Roundtable on the Proxy Process.

Founded in 1946, the Society is a professional membership association of more than 3,600 corporate and assistant secretaries, in-house counsel, outside counsel and other governance professionals who serve approximately 1,700 entities, including 1,000 public companies of almost every size and industry. Society members are responsible for supporting the work of corporate boards of directors and the executive managements of their companies on corporate governance and disclosure matters.

While there are five primary proxy advisory firms in the U.S., today the market is essentially a duopoly consisting of Institutional Shareholder Services (“ISS”), owned by private equity firm Genstar, and Glass Lewis & Co. (“Glass Lewis”), a portfolio company of the Ontario Teachers’ Pension Plan Board. The voting recommendations made by these proxy advisory firms are the single most influential pronouncements each year on the composition of a public company’s board, its executive compensation policies, and an increasingly diverse range of shareholder proposals. The proxy advisory industry is largely unregulated despite compelling evidence of a lack of transparency around firm procedures, issues with the accuracy of information in proxy voting reports, and conflicts of interest. We applaud the SEC’s efforts to consider this issue and, in particular, to explore the checks and safeguards to which proxy advisory firms should be subject to adequately protect the interests of investors and issuers alike.

Recommendations

The Society believes that any review of the U.S. proxy voting process should be approached with the goal of enhancing the transparency surrounding proxy advisory firm practices and procedures. Pursuit of this goal should include requirements that the proxy advisory firms:

- Annually disclose the internal methodologies, guidelines, assumptions and/or rationales used in setting proxy voting policies.

- Adopt a reasonable and transparent comment process prior to setting new, or amending existing, voting policies.
- Clarify whether recommendations are made according to a “generic methodology” rather than a case-by-case approach – for example, by publishing a report of historical voting recommendations on an aggregate basis for each voting policy so investors and other stakeholders can see how the proxy advisory firm generally recommended for all companies.
- Disclose the processes used to gather information, how reviewers are trained and whether recommendations are reviewed by senior managers.
- Provide each public company with a copy of its draft reports in advance of dissemination to proxy advisory firm clients, and provide reasonable response time for the company to review and correct any inaccurate or incomplete factual information in such reports.
- Institute a policy requiring the correction of any factual or other inaccuracies or omissions, as well as redistribution of voting recommendations and re-voting of items relevant to such inaccuracies or omissions.
- Institute an “appeals” process by which an issuer can appeal a decision to a more senior person at the proxy advisory firm to the extent that issuer continues to disagree with a recommendation.
- Provide each company an opportunity to include a response within a proxy voting report relating to any recommendation that is contrary to the management position and is contested as inaccurate or incomplete.
- Report at the end of each proxy season the number of incidents where issuers took exception to the factual statements contained in the proxy advisor’s reports and/or appealed the recommendation of the proxy advisory firm.

The SEC should also reconsider whether proxy advisory firms should be exempt from the proxy solicitation rules (Exchange Act Rule 14a-2(b) (3)) or be subject to other regulation. This would help ensure that fiduciary obligations of good faith and due care are properly carried out by all participants in the process. This can be accomplished by developing a targeted regulatory framework that reflects the unique role that proxy advisory firms perform in the proxy voting process.

We are encouraged by the Division of Investment Management’s recent withdrawal of the no-action letters relating to an investment adviser’s use of proxy advisory firm recommendations. We encourage the Commission to issue new rules or guidance on the fiduciary duties of investment advisers in connection with their use of third-party advisory firm reports. This may include modifications to Staff Legal Bulletin 20 to ensure that reliance on proxy advisory firms remains on a sound basis.

Background

Researchers at George Mason University estimate that ISS and Glass Lewis together have a 97% share of the market for proxy advisory services.¹ ISS employs approximately 1,200 individuals, serves approximately 2,000 institutional clients, and provides proxy recommendations on 42,000 shareholder meetings in 115 countries annually.² Glass Lewis employs 1,200 people, serves over 1,300 institutional clients, and provides voting recommendations on 20,000 shareholder meetings in 100 countries annually.³ Anecdotal evidence from some of our members consistently shows that as much as 30% of the total shareholder votes are cast within 24 hours of the ISS and Glass Lewis recommendations being released to their subscribers, and these votes are typically voted in lockstep with the recommendations. This has resulted in shareholder votes that have become increasingly dependent upon these largely-unregulated firms that, in many instances, exert significantly more influence on the outcome of votes than an issuer's largest shareholder.

One of the Society's central concerns regarding the influence of proxy advisory firms is that unlike institutional investors and corporate management and boards, proxy advisors do not have a fiduciary duty to the clients and shareholders for which they make voting recommendations nor to the corporations about which they are making recommendations. Further, proxy advisory firms are for-profit entities, and therefore have an economic interest in increasing their own profits – not ensuring the economic best interest of the companies they are rating or the shareholders who are often intermediated by investment advisers and custodians voting their shares. As a result, proxy advisors have little incentive to incur costs required to conduct company-specific and high quality inquiries into companies instead of formulating standardized analytical templates to facilitate low cost recommendations on proxy items that may be superficially similar but substantively distinct.

Transparency

Given the high impact of proxy advisory firms' influence on the proxy process, the Society strongly supports greater transparency to shareholders and issuers regarding the services provided and methodologies employed by these firms. While the proxy advisory firm industry should be commended for attempting to improve transparency in recent years, we believe that more needs to be done, including on critical issues such as transparency of firm procedures, accuracy of information used in reports and transparency surrounding proxy firm influence, ownership and other relevant information.

Transparency of Firm Procedures

The Society believes that proxy advisory firms tend to rely on standardized analytical templates that do not adequately assess the specific facts and circumstances of each of the thousands of companies on which they provide recommendations. Although such an approach may maximize profits, it is not well-suited to most cases, including consequential proxy voting decisions on the election of directors and executive compensation matters. While we recognize the efficiency of these generalized strategies, they often result in an ill-fitting one-size-fits-all

¹ James K. Glassman and Hester Peirce, "How Proxy Advisory Services Became So Powerful," Mercatus on Policy Series, Mercatus Center at George Mason University, June 18, 2014.

² See Institutional Investor Services, "About ISS," available at <https://www.issgovernance.com/about/about-iss/>.

³ See Glass Lewis, "Company Overview," available at <http://www.glasslewis.com/company-overview/>.

approach to vote recommendations. It is true that many of ISS and Glass Lewis' voting policies do state that the firms will evaluate company-specific facts, but anecdotal evidence generally indicates a uniform application of certain policies notwithstanding their purported application on a case-by-case basis. By way of example, Society members have reported situations where a proxy advisory firm recommended against a governance practice that had been approved by the company's shareholders in a prior vote or against a proposal intended to provide additional benefit to shareholders – effectively disregarding the will of shareholders. Further, this approach has the compounding effect of homogenizing corporate governance “best practices,” which may benefit the proxy advisory firms themselves, rather than recognizing the variety of legitimate and beneficial governance and corporate practices that are intended to serve the best interest of the beneficial owners.

Currently, proxy advisory firms are largely unregulated, resulting in a lack of transparency. There is no regulatory regime that governs the manner in which these firms develop their policies or form the recommendations or ratings they make. While ISS can be commended for incorporating a public survey of interested parties as part of its annual policy development, there remain issues with this process. For example, while the survey is indeed open to institutional investors, corporate executives, board members and any other interested parties, it is unclear how ISS determines the particular topics, survey questions and response options it publishes for comment each year. Further, ISS does not disclose how it weighs the survey responses in its final policy changes. Notwithstanding their time and effort in participation, companies generally see little evidence that their points of view have been taken into account in ISS' development of its final policies. Thus, it is unclear how ISS actually internalizes the survey responses it does receive, including whether one group of respondents drives the ultimate policy changes or not.

Glass Lewis does not conduct a formalized survey solicitation process, although it does allow stakeholders to provide feedback on its proxy voting guidelines via its website on an *ad hoc* basis and relies on an “independent research advisory council,” which includes limited corporate representation, for feedback on its voting policies. As with ISS, it is unclear how any of the foregoing feedback is ultimately reflected in Glass Lewis' decisions to make policy changes or in the substance of any changes made.

Due Process and Accuracy of Reports and Recommendations

Proxy advisory firms make proxy recommendations on every public company in the United States, and thousands of public companies around the world. The scale and complexity of making proxy voting recommendations for thousands of companies during “proxy season” effectively requires proxy advisors to do all their analysis from February to June, with most recommendations coming out during a 6-to-8-week period.

Reading and accurately digesting thousands of proxy statements, annual reports, and – increasingly – corporate social responsibility and sustainability statements in a condensed time period creates an environment conducive to errors. Given the volume of analysis and the likelihood that errors or misjudgments may occur, it would be reasonable to assume that companies would have the opportunity – indeed, the right – to review and correct any inaccuracies in the proxy voting reports. To the contrary, there is currently no requirement for proxy advisors to provide companies with an opportunity to review and correct voting reports prior to their issuance. As a result, most companies today are not able to see proxy voting reports

about themselves until after each report has been issued. ISS provides its draft proxy voting reports to S&P 500 companies, but provides draft reports to smaller companies only on a discretionary basis or only after the companies have completed a paid subscription to their service. (Concerns regarding these conflicts of interest are discussed below.) Further, any draft report that is provided to a company is accompanied by a very short turnaround time of no more than 72 hours (and often as short as 24 hours) before final publication to ISS' institutional investor clients. Additionally, ISS does not normally provide draft reports for any special meeting or any meeting where the agenda includes a merger or acquisition proposal, proxy fight or "any item that ISS, in its sole discretion, considers to be of a contentious or controversial nature."⁴ Thus, in the situations where an ISS report may be the most consequential, companies often are not able to view a draft at all. Glass Lewis does not provide a copy of its final reports to any public company that does not pay for its reports or otherwise subscribe to its services.

The inability to review draft reports from proxy advisory firms as a matter of right means that companies who want factual errors or omissions corrected are often unable to get a response from proxy advisory firms until it is too late, i.e., until after votes have been cast on the basis of a recommendation that relied – at least in part – on inaccurate or incomplete information.

The Society notes that it has previously relayed its members' concerns about the reporting processes used by proxy advisory firms in its comment letter responding to the SEC's 2010 Proxy Plumbing Concept Release.⁵ Since that time, both ISS and Glass Lewis have improved the ability for issuers to verify the data on which their proxy voting reports are based by providing online verification procedures. However, these confirmation procedures are not consistent between ISS and Glass Lewis. In addition, for companies that are eligible to participate, the procedures require proactive sign-up and are extremely time-bound. For example, ISS' data verification process will be open for 11 days from Nov. 5-16, 2018, and a separate sign-up is needed to verify equity plan data (which opens generally around 12 days after the filing of the company's proxy materials). It is worth noting that ISS' data verification protocol is applicable only to its so-called Quality Score, not the firm's proxy voting report⁶, which contains the actual proxy voting recommendations that drive a significant share of investor voting. Separately, Glass Lewis' "Issuer Data Report" can be accessed only after a company signs up through its Meetyl platform. The Issuer Data Report is then issued three to four weeks before the company's annual meeting, at which time companies have only 48 hours to respond. While these verification procedures have been welcomed by the Society, we believe the better solution is for companies to have the opportunity to view the recommendations before they are distributed.

Even in instances where a company has been able to respond in the limited contexts and time periods allotted, there remain concerns about proxy advisory firms' correction of factual errors and omissions and their failure to change voting recommendations after "corrections" have been made. Because factual errors are typically found after the voting recommendation has been disseminated to the thousands of institutional investors who subscribe to ISS and Glass Lewis' services, the ability to "pull back" the inaccurate data is limited. Neither advisor makes a firm commitment to correct errors, omissions or misstatements in reports, and no explanation is

⁴ <https://www.issgovernance.com/contact/faqs-engagement-on-proxy-research/>

⁵ <https://www.sec.gov/comments/s7-14-10/s71410-272.pdf>

⁶ <https://www.issgovernance.com/file/faq/how-to-verify-your-qualityscore-data-november-2017.pdf>

guaranteed regarding a refusal to correct an error. If ISS agrees that it has made a “material error that should be brought to clients’ attention,” it will promptly issue an “Alert” report to all its “relevant clients.”⁷ Which clients are relevant is undefined, and investors who download reports and/or use Artificial Intelligence to scan documents for incorporation into voting analysis and strategies may not pick up such “Alerts.” It is also unclear if such corrections impact ISS’ voting recommendations, or if votes cast based on incorrect recommendations are ever highlighted and changed.

We note that some Society members have indicated that their institutional investors were unaware of a mistake in a report and stated that if they had known otherwise, their votes would have been different. Other Society members, representing small or mid-cap companies, do not receive proxy advisory firm reports at all and thus are placed at a significant disadvantage in their ability to begin to assess the basis upon which votes may have been made by their institutional investors.

When a company does find out about an incorrect negative recommendation, the results can be costly and damaging. A very real example of this problem, detailed in [Appendix A](#), comes from a Society member that works for a small cap company in the transportation industry.

Finally, we note that proxy advisory firms do not disclose publicly the overall rate of requested or actual corrections to their proxy reports or the rate of reported errors in their proxy voting services such that it is impossible for investor clients, companies, the SEC or academic researchers to assess firm performance in this regard.

Conflicts of Interest

ISS’ business model includes a foundational conflict of interest—it provides clients with voting recommendations on a company’s corporate governance and compensation policies and also seeks to be hired by these same companies to provide paid corporate governance and/or compensation consulting services.

Society members have reported being contacted by ISS’ corporate consulting sales force suggesting that they have a unique ability to help fix any problems that the company has had with a previous vote if they hire ISS for a consulting engagement. And in these conversations with the sales force, companies are offered a tiered service level where more ISS involvement and insights come at a higher price. In addition, ISS now offers an environmental scorecard consulting service, for an added cost.

A conflict of interest applicable to all proxy advisors is that such firms provide voting recommendations on shareholder proposals that may have been submitted by their institutional investor clients without disclosing that such a conflict exists. Further, ISS has a paid service for shareholder proponents to help them craft proposals that will pass muster under SEC rules. In addition, proxy advisors also sell data and other analytical tools to institutional investors and hedge funds⁸, and then simultaneously recommend votes on all matters, including these same hedge funds’ proxy contests.

⁷ <https://www.issgovernance.com/contact/faqs-engagement-on-proxy-research/>

⁸ <https://www.sustainalytics.com/press-release/sustainalytics-glass-lewis-corporate-governance-data-services-offering/>

These conflicts should be specifically and prominently disclosed to institutional investor clients in voting reports so that they may evaluate this information in the context of the proxy advisors' voting recommendations.

Proxy Advisory Firm Influence

Proxy advisory firms are one of the few participants in the proxy voting process that are not generally required to be registered or regulated by the SEC. Proxy statements are subject to regulation under the Securities Exchange Act of 1934 (including liability thereunder for misstatements or omissions); proxy advisory firm reports, however, are not. Yet, many institutional investors rely upon them just as heavily, if not more so, in making voting and investment decisions. There is little accountability by proxy advisory firms, even though, as discussed previously, they have a significant impact on so-called “routine” (albeit, critical) matters at widely held companies and decisively swing the vote in many situations.

Proxy advisory firms' outsized influence is more prevalent with smaller passive investors, quantitative fund managers, or those who simply own one stock as a hedge against another position. Such investors simply do not have an incentive to devote the resources or expertise to in-house proxy staffs to analyze and vote at the numerous shareholder meetings. Large asset managers like BlackRock, Vanguard, T. Rowe Price, State Street Global Advisers, TIAA-CREF, BNY Mellon, Capital Group, and other well-known and well-resourced firms—tend to view proxy voting as core to their overall asset management strategy. They have large teams of associates whose only responsibility is to engage with companies on corporate governance matters, to analyze the company's policies and proxy statements, and to make vote recommendations based on the manager's mandate. Their voting processes utilize many data points, including proxy voting reports, typically as a screen or filter, but they also conduct a deeper analysis on companies that deviate from their own (tailored) policies, which form the basis for the “custom guidelines” that they instruct the proxy advisory firms to use when voting their shares. Moreover, they engage with many corporations and their governance teams.

However, the Society believes many small and mid-size institutional investors and managers outsource their voting decisions to proxy advisory firms that provide automated voting services to fulfill what they believe to be their proxy voting compliance obligations at the lowest cost. Together, these small managers can represent a significant ownership level. A number of these small managers adopt ISS and Glass Lewis “default” voting guidelines and policies and then let the proxy firms apply these policies by generating electronic ballots that reflect these default positions for each shareholder meeting. As a technical matter, the client has the right to override a specific voting recommendation, but most of these ballots are left untouched and submitted automatically without any client input or decision.

The U.S. Chamber of Commerce's Center for Capital Markets Competitiveness and Nasdaq conducted a survey of the 2018 proxy season in which 165 public companies participated.⁹ This survey found that large percentages of shares voted in line with proxy advisory firm recommendations. Specifically with ISS, several companies responded that 10-15% of shares voted automatically in line with ISS' recommendations within the 24-hour period

⁹ U.S. Chamber of Commerce's Center for Capital Markets Competitiveness and Nasdaq, “Proxy Season 2018: Examining Developments and Looking Forward,” *available at* https://www.centerforcapitalmarkets.com/wp-content/uploads/2018/10/ProxySeasonSurvey_v3_Digital.pdf.

following the issuance of its recommendations, and others estimated that between 25-30% voted in lockstep with ISS during that time period, certainly more than enough impact to swing the outcome on many votes. The correlation with Glass Lewis is less apparent, but Glass Lewis offers a product to its clients that votes their shares in line with its report recommendations two days before the issuer's annual meeting, which means more shares are likely voted lockstep with the recommendations than the survey revealed.

This influence directly and significantly affects matters up for a vote at annual meetings. For example, in 2012, ISS recommended “against” a lobbying disclosure shareholder proposal that was put to a vote at the annual meeting of one Society member, and fewer than 10% of shares voted to support the proposal. The following year, the same lobbying disclosure shareholder proposal was submitted to a vote at the annual meeting. However, ISS changed its policies with respect to these types of proposals and switched its recommendation to vote “for” the proposal, resulting in more than 24% of shares voted in support of the proposal. Year to year, there was no change in the issuer’s lobbying practices or disclosure, and the make-up of the company’s institutional shareholders had changed minimally. This nearly 15% swing in the vote outcome is clearly attributable to ISS’ changed recommendation, and is consistent with the information above regarding ISS exercising control over the company’s votes cast.

For one Society member company that tracked the voting timing impact following the issuance of ISS’ voting report in 2018 and 2017, an estimated 13.1% and 9.3% of the total votes cast in 2018 and 2017, respectively, were cast lockstep with ISS’ recommendations within one business day after the release of ISS’ report. By comparison, the percentage of votes cast on other business days just before the release of the ISS report typically fell between 0.2% and 0.3% of the total votes cast in the annual meeting. To put all of this into proper perspective, the voting block essentially controlled by ISS’ recommendations has more influence on the voting results than this company’s largest shareholder.

This example highlights shares voted in line with proxy advisory firm recommendations within the 24-hour period following the release of proxy voting reports. When institutions are voting in lockstep with these recommendations following this initial period after the research report is issued, it is not possible to quantify this voting because institutions are not required to publicly disclose when they in essence “outsource” decision-making over proxy matters to third parties. We can surmise, however, that the proxy advisory firm influence may be greater than we can quantify with available data.

Concerns about the influence of proxy advisory firms are not limited to corporations. There is industry-wide consensus that proxy advisory firm recommendations are impacting the corporate governance landscape in a way that warrants information “users” (i.e., the firms’ investor clients) to exercise self-restraint and caution. In 2016, a group representing some of the United States’ largest corporations and institutional investors published the “Commonsense Principles of Corporate Governance”, in an effort to find common ground recognizing that the “long-term prosperity of millions of American workers, retirees and investors depends on the effective governance of our public companies.” In the most recent update published in October 2018, the Principles stated, “Asset managers may rely on a variety of information sources to support their evaluation and decision-making processes. While data and recommendations from proxy advisors may form pieces of the information mosaic on which asset managers rely in their analysis, ultimately, their votes should be based on independent application of their own voting

guidelines and policies. *To the extent they use recommendations from proxy advisors in their decision-making processes, asset managers should disclose that they do so, and should be satisfied that the information upon which they are relying is accurate and relevant. Proxy advisors whom they use should have in place processes to avoid or mitigate conflicts of interest.*¹⁰ (2018 language italicized.)

Our recommendations are entirely consistent with this view.

Fiduciary Obligation in Making Voting Decisions

SEC rules require investment companies and investment advisers to adopt policies and procedures to ensure that proxies are voted in the best interests of their shareholders and clients.¹¹ Based on the data above, we believe it appropriate for the Commission to examine in more detail whether some investors are overly relying on proxy advisory firms (e.g., to third parties that do not bear any responsibility for, or share any economic risk with regard to, the issuer in question). As noted by the Commission, “institutional investors, whether relying on proxy advisory firms or not, must vote the institutions’ own shares and, in doing so, must discharge their fiduciary duties to act in the best interest of their investors and avoid conflicts of interest; institutions are not relieved of their fiduciary responsibilities simply by following the recommendations of a proxy advisor.”¹² Similarly, in 2016, the Department of Labor noted that when pension plan fiduciaries vote, they have a duty to consider only the factors that relate to the economic value of the plan’s investment and shall “not subordinate the interest of the participants and beneficiaries in their retirement income to unrelated objectives.”¹³ This clearly supports the notion that these investors have a fiduciary duty to vote in a way to maximize the economic value of their fund. ISS has no such duty and makes its recommendations in accordance with its own views of best practices, not the economic interests of the funds’ clients. Therefore, if overly relying on a proxy advisor for its voting responsibility, an investor may effectively be delegating its voting responsibilities to a non-fiduciary.

Regulatory Consistency

While Section 13 of the Securities Exchange Act of 1934 and related rules require shareholders with beneficial ownership of more than 5% of voting stock of a company to disclose their holdings and other specified information on a Schedule 13D or 13G, proxy advisory firms are not subject to similar disclosure requirements. Shareholders subject to Schedule 13D disclosure in particular are required to make specified disclosures regarding the identity of all persons who form a “group” with them with respect to such stock ownership, the purpose for their acquisition of the stock and any contracts, arrangements, understandings or

¹⁰ <https://www.governanceprinciples.org>

¹¹ Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, SEC Release No. IC-25922, 68 Fed. Reg. 6,564 (February 7, 2003), available at <http://www.sec.gov/rules/final/33-8188.htm>; and Proxy Voting by Investment Advisers, SEC Release No. IA-2106, 68 Fed. Reg. 6,585, available at <http://www.sec.gov/rules/final/ia-2106.htm>.

¹² SEC Release No. 34-60215 (approving amendments to NYSE Rule 452), July 1, 2009, p. 26, available at <http://www.sec.gov/rules/sro/nyse/2009/34-60215.pdf>.

¹³ Interpretive Bulletin Relating to the Exercise of Shareholder Rights and Written Statements of Investment Policy, Including Proxy Voting Policies or Guidelines, December 29, 2016, available at <https://www.dol.gov/sites/default/files/ebsa/2016-31515.pdf>.

other relationships with respect to the stock. In addition, shareholders must promptly update the Schedule 13D for material changes. However, even though the two largest proxy advisory firms each effectively control a voting bloc that is much larger than the Schedule 13D threshold (5%), they are not subjected to a comparable regulatory regime.

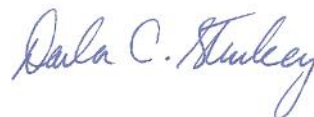
Proxy advisory firms instead operate under a patchwork regulatory system. ISS has registered as an investment adviser, but no other firm has. Glass Lewis is not registered as an investment adviser (or under any other securities statute), and is not currently subject to any regulatory supervision. Additionally, the SEC has created an exemption from its proxy rules for proxy advisory firms, so they are not required to abide by solicitation and disclosure rules that apply to other proxy participants.

Conclusion

The debate concerning the proper role and regulation of proxy advisory firms has been underway for some time. We are grateful that the SEC has scheduled the Staff Roundtable and will review proxy advisory firms. The Society's recommendations (pp.1-2) are intended to provide investors and issuers with greater confidence that the most important recommendations on matters of corporate governance are in shareholders' and the broader economy's best interests.

We appreciate the opportunity to provide comments on the proxy process and proxy advisory firms and would be happy to provide you with further information to the extent you would find it useful.

Respectfully submitted,

A handwritten signature in blue ink that reads "Darla C. Stuckey". The signature is written in a cursive, flowing style.

Darla Stuckey
President and CEO
Society for Corporate Governance

Appendix A

In May 2016, we received an ISS report with an ‘against’ recommendation regarding Say-on-Pay that was based on a material factual error. The ISS personnel incorrectly concluded that under our annual bonus plan, we set the financial metric goal for the 2015 fiscal year lower than the actual results we had obtained in 2014. This was simply untrue—this was not a matter of methodology or interpretation, but a clear mathematical mistake.

As a small-cap company, unlike larger companies, we are not given a ‘preview’ of our report from ISS, so we received this report just 2 weeks prior to our May 2016 annual meeting. We quickly utilized all of the methods available to us to try to get the error corrected and the recommendation reversed. Although ISS acknowledged the error, they declined to issue either a correction or a revised report.

We engaged in robust shareholder outreach as we have for many years, and while the shareholders who were able to speak with us quickly understood the mistake and supported our Say-on-Pay [proposal], we were not able to have meetings with all the shareholders we reached out to due to the extremely busy proxy ‘inseason’ and a large portion of our shareholders being quantitative or passive firms who outsource their voting to proxy advisory firms. The result was that our 2016 Say-on-Pay [proposal] narrowly failed with a 49.8% favorable vote outcome.

We engaged in extensive ‘offseason’ shareholder outreach during the fall of 2016, reaching out to shareholders representing over 75% of our outstanding shares, and, while shareholders offered small governance-related suggestions such as proxy access, none expressed any wish to see specific changes in our executive pay program; some instructed us to ‘fix’ our ISS recommendation and then they would be sure to vote in support. We promptly added proxy access, and disclosed our outreach efforts and feedback in our April 2017 proxy statement fully and accurately.

In May 2017, ISS issued their report, again recommending against our Say-on-Pay, alleging that due to our prior year’s low vote outcome, our shareholders must have demanded extensive pay program changes that our compensation committee ignored. This was simply factually untrue.

Due to ISS’ programmatic rules, a second consecutive year meant ISS not only recommended against Say-on-Pay but against the re-election of our four-member compensation committee, including a new committee member who was not even on the board at the time compensation decisions were being made. This meant that four members of our ten-member board who had been key drivers of an extraordinary 2016 business year that saw a transformative transaction with a global e-commerce company and a 26% shareholder return were at risk of non-re-election due to proxy advisory errors and formulaic inflexibility. Moreover, the board members being recommended against included at the time the sole female member of our board and one of our two racially diverse board members.

Thanks to above-and-beyond shareholder outreach efforts, we were able to get the compensation committee members re-elected but received only 32% in favor of our Say-on-Pay vote in May 2017.

Through a combination of extensive pro-active compensation program changes and at-length engagement with ISS and Glass Lewis in the fall of 2017, this May we received ‘for’ recommendations from both firms in reports which were fortunately finally absent material factual errors (ISS’ report still has an error regarding our perquisite program which we are attempting to fix). This recommendation resulted in a 94% favorable Say-on-Pay vote this year, demonstrating the outsize influence of proxy advisory firms and the crucial need for regulation that ensures shareholders who rely on proxy firms’ recommendations are relying on accurate data.¹⁴

¹⁴ <https://www.banking.senate.gov/imo/media/doc/Stuckey%20Testimony%206-28-18.pdf>