

Client Alert

ISS Issues Final 2012 Policies

EXEQUITY

Independent Board and
Management Advisors

On November 17, 2011, Institutional Shareholder Services Inc. (ISS) issued *final* 2012 Policies.¹ The final policies do not appear to stray that far from the draft policies released back in October 2011,² but there were a few portions of the policies of interest:

- **Pay-for-Performance (P4P) Alignment**—Virtually identical to the draft policy that was issued in October 2011. ISS still offers few details about how it will create peer groups for purposes of its P4P alignment analysis and determine how a company gets slotted into a particular P4P alignment group (i.e., strong, weak, or “aligned”). The only information ISS offers on how peer groups will be selected for purposes of its P4P assessment is in footnote 1 on page 9 of the 2012 Policy Updates, which says, “The peer group is generally comprised of 14–24 companies that are selected using market cap, revenue (or assets for financial firms), and GICS industry group, via a process designed to select peers that are closest to the subject company, and where the subject company is close to median in revenue/asset size.”³

Exequity Comment: ISS also eliminated the existing exception to the P4P policy for “new” CEOs (CEOs who did not serve in that position for a full two fiscal years).⁴

- **Say on Pay (SOP) Proposals That Receive Less Than 70% of Votes Cast in Favor**—Such proposals will trigger additional scrutiny under the ISS Management SOP Policy which can cause ISS in the year following such vote to recommend against compensation committee members (or, in rare cases, the full board) and the next SOP proposal. ISS has identified factors it will take into account and has indicated that support levels of less than 50% will warrant the highest level of company responsiveness.
- **Say When on Pay/SOP Frequency**—ISS adopted the proposed policy that indicates that ISS might consider recommending **against** or **withhold** from the entire board (except new director nominees) if the board implements an SOP frequency that is less frequent than the frequency that received a plurality, but not a majority, of the votes cast. In making its recommendation, ISS will consider the board’s rationale for such action, the company’s ownership structure and vote results, its own analysis of whether there are compensation concerns or a history of problematic compensation practices, and the previous year’s support level on the company’s SOP proposal.

Exequity Comment: The final policy eliminated one of the factors that the draft policy indicated ISS would take into account, i.e., the difference between the frequency adopted and the frequency supported by shareholders.

¹ These final policies are available at <http://www.issgovernance.com/policy>.

² See our *Client Alert*, “ISS Issues Draft 2012 Policies” (October 20, 2011), available at: http://www.exqty.com/Media/Publications/ISS%20Draft%202012%20Policies_20111020.pdf for a full discussion of these policies.

³ *U.S. Corporate Governance Policy, 2012 Updates* (November 17, 2011), p. 9, footnote 1, available at: http://www.issgovernance.com/files/ISS_2012US_Updates20111117.pdf.

⁴ *Ibid.* p. 11.

ISS indicated that it received only 49 comments on its draft policies—23 from institutional investors, 18 from corporate issuers, and 8 from advisors or other organizations. ISS indicated that most commentators viewed the 2012 policies as improvements, but corporate issuers and a few investors raised concerns about peer group selection, sole use of total shareholder returns, and transparency of the policies.

Additional Guidance on 2012 Policy Methodologies

In response to these concerns, while ISS finalized its proposed P4P alignment policy, ISS did state that it will release a technical document in December 2011 that will provide its P4P methodology for 2012.⁵ Additionally, ISS stated that it will disclose its peer group methodology prior to the 2012 proxy season so that institutional shareholders and corporate issuers can understand how ISS will construct peer groups. Unfortunately, until this additional guidance is provided, corporate issuers will be left with more questions than answers regarding ISS's 2012 policies.

Exequity Comment: *Until ISS issues this technical guidance, ISS's 2012 P4P policy will be a black box. Once ISS issues this guidance, we will be able to provide a more robust analysis of the implications for corporate issuers of the 2012 Policy Updates.*



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⁵ 2012 Corporate Governance Policy Updates and Process, Executive Summary (November 17, 2011), p. 4, available at: http://www.issgovernance.com/files/ISS_2012ExecutiveSummary20111117.pdf.

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