

## ISS Releases 2012 Policy Updates

On November 17, ISS published its annual update to its U.S. Corporate Governance Policy. These updates are certain to have an impact on voting in the upcoming 2012 proxy season, although the precise impact cannot be predicted. ISS has maintained a “case-by-case” approach to many of the significant issues. In that context, however, significant policy changes for this year include:

- **Proxy Access.** ISS generally supports proxy access proposals as “an important shareholder right.” It will analyze proxy access proposals on a case-by-case basis, taking into account unspecified “company-specific factors,” as well as factors specific to the proposal, such as ownership thresholds (percentage and holding period) to gain access, the maximum proportion of directors and, in the case of multiple nominations, the method of determining whose nominations will appear in the proxy. The policy updates do not give any indication of where ISS would come out on any of the proposal-specific factors.
- **Voting for Directors in Uncontested Elections.** Currently ISS votes against or withholds from directors individually for “material failures of governance, stewardship, or fiduciary responsibilities,” for “failure to replace management as appropriate,” and for “egregious actions related to the director’s service on other boards” that raise substantial doubt about the ability to oversee management. The 2012 update simply adds risk oversight to the items the material failure of which will result in a withhold position.
- **Response to Say on Frequency Votes.** ISS will vote against or withhold from the entire board of directors if it adopted a frequency policy other than the one that received a majority of the votes cast at the last annual meeting. It will vote on a case-by-case basis in situations where the frequency chosen was other than the one that received a plurality of the votes cast at the meeting. Factors it will consider in this circumstance include the company’s rationale for the choice, the company’s ownership structure and voting results, ISS’ analysis of whether there are any compensation concerns at the company and the support level on last year’s say-on-pay proposal.
- **Board Response to High Levels of Say-on-Pay Opposition.** ISS will vote on a case-by-case basis on Compensation Committee members (or in exceptional cases the entire board) if the previous year’s say-on-pay proposal received the support of less than 70% of the votes cast. ISS will take into account:
  - The company’s response, including:
    - Disclosure of engagement efforts with major institutional investors
    - Specific actions to address the issues that led to the low support level
    - Other compensation actions the company has taken
  - Whether the issues are isolated or recurring
  - The company’s ownership structure (although the update is not clear on how this factors in)
  - Whether the support level was below 50%, where ISS expects the highest level of responsiveness

- **Say-on-Pay Votes.** ISS has refined its methodology for determining pay-for-performance alignment. For Russell 3000 companies, ISS considers:
  - Peer group alignment. The methodology for 2011 involved looking at the company's total shareholder return (TSR) in relationship to its entire four-digit GICS group. For 2012, the peer group will be narrowed to 14-24 companies within the GICS group that are selected based on market cap and revenue (or assets for financial firms), where the subject company is close to the median on those metrics. Alignment considers one- and three-year pay and total shareholder return (TSR) within the peer group and the CEO's pay relative to the median of the group. One-year performance has a 40% weight and three-year performance has a 60% weight.
  - Absolute alignment. ISS analyzes the trend in CEO pay and the company TSR over the past five years.

If this analysis reveals unsatisfactory alignment, or for non-Russell 3000 companies misalignment is "otherwise suggested," then ISS will look at various factors to determine how they work to encourage or undermine long-term value creation:

- Ratio of performance- to time-based awards
  - Ratio of performance-based compensation to total compensation
  - Completeness of disclosure and rigor of performance goals
  - Peer group benchmarking practices
  - Actual financial results
  - Special circumstances (they cite as two examples a new CEO or biennial grant practices)
  - Any other relevant factors
- **Incentive Bonus Plans and 162(m) Proposals.** For companies that presented plans for Section 162(m) approval following their IPO, the ISS position has historically been to support the proposal. ISS is changing this position and will now perform a full equity plan evaluation the first time a plan is presented for 162(m) approval.

ISS also announced various other policies on governance and social/environmental issues, which can be accessed [here](#).

ISS' influence in proxy voting is unlikely to diminish during the next proxy season. Companies should review any of the guidance applicable to them and factor it into their 2012 planning.

Please contact your usual Ropes & Gray adviser with any additional questions about the ISS 2012 Policy Updates.