

November 23, 2015

ISS and Glass Lewis Update Their Proxy Voting Guidelines for the 2016 Proxy Season

Institutional Shareholder Services Inc. (ISS) and Glass, Lewis & Co. (Glass Lewis) have both released updates to their respective proxy voting guidelines.¹ This alert provides a brief summary of the significant changes to each proxy advisory firm's respective policies for the 2016 proxy season. ISS's revised policies will take effect for annual meetings that are held on or after February 1, 2016, while Glass Lewis's revised policies will apply to meetings that are held on or after January 1, 2016.

Key Updates to ISS's Proxy Voting Guidelines

After concluding its annual global policy review, consisting of a policy survey, a request for comments on proposed policy changes, and several roundtable discussions, ISS issued its policy updates for the 2016 proxy season. Below is a summary of the key policy updates applicable to U.S. companies.

Proxy Access

ISS stated that its fundamental approach to management and shareholder proxy access proposals remains unchanged. ISS also acknowledged that, while it is unlikely that many proxy access director nominees will appear in 2016, it plans to update the framework that it will use to evaluate such nominees. ISS indicated that it will release a FAQ document in December 2015, which will provide more information on which additional proxy access provisions ISS considers overly restrictive as well as details regarding the analytical framework that it will use to evaluate proxy access director nominees.

Overboarding

ISS currently considers a director "overboarded" if he or she sits on more than six public company boards – or, if he or she is also a CEO, more than three public company boards (including the "home" company board). Under the new policy, ISS reduced the maximum number of public company boards that a director who is not also a CEO can sit on from six to five. There will be a one-year grace period before directors are evaluated under this new policy until 2017. During this grace period, ISS research reports will highlight if a director serves on more than five public company boards, but ISS will not make an adverse voting recommendation unless the current maximum of six boards is exceeded. For CEOs, the current overboarding limit will remain at two outside directorships. While ISS decided not to change this policy with respect to CEOs, it noted that it will continue to study the issue.

Unilateral Governance Changes

With regard to board actions that significantly reduce shareholder rights without approval by shareholders (so-called unilateral board actions), ISS's policy is being updated to distinguish between (1) unilateral board adoptions of bylaw or charter provisions made prior to or in connection with a company's initial public offering (IPO), and (2) unilateral board amendments to those documents made after a company's IPO. According to ISS, this distinction better reflects the differing expectations that investors may have for newly public companies versus more established public companies.

¹ ISS, [2016 Policy Updates](#) (Nov. 20, 2015); Glass Lewis, [Proxy Paper Guidelines, 2016 Proxy Season: An Overview of the Glass Lewis Approach to Proxy Advice – United States](#) (Nov. 13, 2015).

- For newly public companies, under ISS's updated policy, it will give significant weight to shareholders' ability to change the governance structure in the future through a simple majority vote, and their ability to hold directors accountable through annual director elections. A public commitment by the company to put the adverse provisions to a shareholder vote within three years of the IPO can also be a mitigating factor.
- For established public companies, the updated policy generally calls for continuing to withhold votes from directors who have unilaterally adopted provisions that create a classified board, establish supermajority voting requirements to amend the company's bylaws or charter, or eliminate shareholders' ability to amend bylaws.

Further, in subsequent years and on a case-by-case basis, ISS will consider these adverse governance provisions in determining vote recommendations for director nominees until such time as the actions are reversed or submitted to a shareholder vote.

Key Updates to Glass Lewis's Proxy Voting Guidelines

Conflicting Management and Shareholder Proposals

In light of the significant limits that SEC Staff Legal Bulletin No. 14H (SLB 14H) placed on the applicability of Rule 14a-8(i)(9),² which permits a company to exclude a shareholder proposal that directly conflicts with a company's own proposal, Glass Lewis acknowledged that "some companies may still choose to place management proposals alongside similar shareholder proposals." Glass Lewis's updated policies therefore include guidance on how it would evaluate whether to support a "conflicting" management proposal, which includes the consideration of the following factors:

- the nature of the underlying issue;
- the benefit to shareholders from implementation of the proposal;
- the materiality of the differences between the terms of the shareholder proposal and management proposal;
- the appropriateness of the provisions in the context of a company's shareholder base, corporate structure, and other relevant circumstances; and
- a company's overall governance profile and, specifically, its responsiveness to shareholders as evidenced by the company's response to previous shareholder proposals and its adoption of progressive shareholder rights provisions.

Last year, seven companies included competing management and shareholder proxy access proposals in their proxy statements (representing approximately 8% of the proxy access proposals that were voted on in 2015).³ It is unclear, however, what effect SLB 14H will have on the number of companies that will include a competing proxy access proposal in their proxy statements for the 2016 proxy season.

Director Overboarding Policy

Similar to ISS, Glass Lewis announced changes to its director overboarding policy and will also provide companies with a one-year grace period. As a result, Glass Lewis's voting recommendations in 2016 will continue to be based on its existing thresholds of three total boards for a director who serves as an executive officer of a public company

² For a detailed analysis of SEC Staff Legal Bulletin No. 14H, please refer to our previous Alert, "[SEC Issues Staff Legal Bulletin Outlining the Scope of the 'Directly Conflicts' Exclusion under Rule 14a-8 and Providing Guidance on the Staff's Interpretation of the Ordinary Business Exclusion](#)" (Oct. 26, 2015).

³ Management proposals at three companies (Exelon Corporation, Expeditors International of Washington, Inc., and SBA Communications Corporation) passed, shareholder proposals at three companies (AES Corporation, Cloud Peak Energy Inc., and Visteon Corporation) passed, neither the management nor the shareholder proposal passed at one company (Chipotle Mexican Grill, Inc.), and there were no companies where both proposals were passed.

and six total boards for directors who are not public company executives. For meetings held in 2016, Glass Lewis will note as a concern instances of a director serving as an executive of a public company while serving on more than two boards and any other director who serves on more than five total boards. Beginning in 2017, Glass Lewis's voting recommendations will be based on these lowered thresholds.

Exclusive Forum Provisions

Glass Lewis changed its approach to companies that include exclusive forum provisions in their governing documents in connection with an IPO and will no longer recommend that shareholders vote against the chairman of the nominating and governance committee in such situations. Instead, Glass Lewis indicated that it will weigh the presence of an exclusive forum provision in a newly public company's bylaws along with other provisions that it believes will unduly limit shareholder rights, such as supermajority vote requirements, a classified board, or a fee-shifting bylaw.

Companies that are considering whether to seek shareholder approval of an exclusive forum provision should note that Glass Lewis's current policy is to generally recommend that shareholders vote against any bylaw or charter amendment seeking to adopt such a provision. Glass Lewis may consider supporting the adoption of such a provision, however, if the company provides a compelling argument on why the provision would directly benefit shareholders, provides evidence of abuse of legal process in other, non-favored jurisdictions, has narrowly tailored such provision to address the risks involved, and has maintained a strong record of good corporate governance practices.

Environmental and Social Risk Oversight

Glass Lewis codified its policy regarding the responsibilities of directors for the oversight of environmental and social issues. Glass Lewis believes that boards should ensure that management conducts a complete risk analysis of company operations, including those that have environmental and social implications. Where the board or management has failed to sufficiently identify and manage a material environmental or social risk that did or could negatively impact shareholder value, Glass Lewis will recommend that shareholders vote against the directors responsible for risk oversight.

Nominating Committee Performance

Glass Lewis clarified its guidelines to indicate that it may consider recommending that shareholders vote against the nominating committee chair where the board's failure to ensure that the board has directors with relevant experience, either through periodic director assessment or board refreshment, has contributed to a company's poor performance.

Compensation Updates

Glass Lewis provided a more detailed discussion of how it will analyze awards granted to newly hired executive officers and generally reiterated its positions with respect to discretionary, one-time awards. With respect to one-time awards, Glass Lewis requires a thorough description of the awards and an explanation of why they are necessary and why existing awards do not provide sufficient motivation. Sign-on arrangements should be clearly disclosed and accompanied by a meaningful explanation of the payments involved and the process by which the amounts were reached. In addition, the details of any "make-whole" awards should be provided. Glass Lewis also added minor clarifications regarding its analysis of equity compensation plans.