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IPO Governance Gains Investor Attention

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CII issued a recent policy statement focused on newly public companies, prompted by concerns about high-profile IPOs using dual-class shares. In 2015, dual-class IPOs raised twice as much capital compared to the prior year.

Companies going public are urged to avoid the following structures, either at the outset or by changing them over a period of time through the use of a “sunset” mechanism:

- Multi-class equity structure with unequal voting rights;
- Plurality vote requirement for uncontested director elections;
- Lack of independent board leadership, whether the chair or lead director;
- Classified board structure; and
- Super-majority vote requirements for bylaw amendments and other proposals.

The interest in dual-class companies intensified recently as Reuters reported that T. Rowe Price plans to vote against key directors, such as the lead independent directors, independent chairs and all of the nominating and corporate governance committee members, at companies with dual-class stock. The investor’s policy does not appear to be limited to IPO companies.

Like CII, both proxy advisory firms have increased their focus on IPO governance structures with updated 2016 policies. ISS will now recommend voting against directors if IPO companies adopt bylaw or charter provisions that are viewed as impairing shareholder rights, most notably classified boards and restrictions or supermajority requirements for shareholders to amend charters or bylaws. Companies can mitigate these issues by agreeing to put the provisions to shareholder vote within three years. Otherwise, unlike many other ISS policies where an adverse recommendation is only made in the first year, ISS may continue to recommend against directors in subsequent years.

Glass Lewis generally provides a one-year grace period immediately following an IPO, but will recommend against a board that adopts a poison pill or classified board prior to IPO unless the board commits to submitting the classified board to a vote within 12 months and the pill sunsets in three years or less.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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