

New Defensive Tactic Leads to Negative Recommendations for Director Elections

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In response to concerns about the seeming prevalence of activist attention, at least 26 companies since May have adopted bylaws that prohibit as candidates for directors those who are parties to any compensatory, payment or other financial arrangements with anyone other than the company.

Now, ISS is recommending against the nominating and governance committee of Provident Financial, the first company of the bunch that is holding its annual meeting. ISS criticizes the company for the “unilateral adoption of a bylaw amendment that significantly impacts shareholders’ rights,” because it would “unduly restrict investors’ ability to nominate and elect otherwise qualified individuals via a proxy contest.” ISS also believes that the board could have put the matter to shareholder vote.

ISS distinguishes companies with similar bylaws that focus only on the lack of disclosure of such payments, as well as the controversy surrounding proxy contests at Agrium and Hess, where potential conflict issues were raised over the prospect of dissident nominees who would have been provided incentive awards if they had won election. By contrast, the Provident-type bylaw is viewed by ISS as particularly onerous because it affects nominees during their candidacy, and those nominees often receive a reasonable fee for agreeing to stand for election in a contest.

This likely comes as a surprise for the companies that have adopted the bylaws because there is no specific ISS policy addressing this matter, since it has not previously been an issue. Instead, the ISS recommendation stems from its catch-all policy that it will recommend against individual directors, committees or even the entire board for “material failures of governance, stewardship, risk oversight or fiduciary responsibilities at the company.” It is also a good reminder that ISS does review a company’s filings other than the proxy statement, as the Provident bylaw was disclosed in an 8-K during the past summer.

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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