

ISS Issues FAQs on Its New Independent Chair Proposal Policy

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ISS recently issued new FAQs on its 2015 policy updates. As we discussed in [our memo](#), a key change relates to how ISS will make recommendations for companies with shareholder proposals seeking independent chairs for boards of directors.

Like the policy update, the [FAQs](#) emphasize that the new approach adopts a holistic review using various factors in determining a recommendation. For example, previously if a company had a lead director with a set list of duties and met the other specific policy criteria, the company could be certain that ISS would recommend “against” the proposal.

Under the updated policy, having a designated lead director with what ISS considers robust responsibilities is still an important factor, but will not be dispositive. Other considerations with respect to board leadership structure will also include: the presence of an executive or non-independent chair in addition to the CEO; a recent recombination of the role of CEO and chair; departure from a structure with an independent chair; and any recent transitions in board leadership and the effect such transitions may have on independent board leadership. The duties that ISS believes should be assigned to lead directors in order to be considered robust have not changed, but under the holistic review, ISS appears to be more flexible in not requiring that the lead director must have all of them.

Another factor that will be weighed is board tenure, in terms of concurrence of director/CEO tenure, lengthy directorships, or high average director tenure. Company performance was previously considered, but ISS has also added five-year TSR to its review of one- and three-year TSR. Performance over the long-term will be weighed more heavily than short-term performance. While no single criterion is designed to be decisive, performance is noted to be a “significant” factor in the overall holistic analysis.

ISS will also examine a company’s governance practices, and those that will be viewed negatively include: problematic compensation practices; multiple related-party transactions or other issues putting director independence at risk; failures of risk oversight; adoption of shareholder-unfriendly bylaws without seeking shareholder approval; failure of a board to adequately respond to majority-supported shareholder proposals or directors who do not receive majority support; and “flagrant actions” by management or the board with potential or realized negative impacts on shareholders.

A company’s disclosure on why it opposes the shareholder proposal and its rationale for maintaining a non-independent chair will be considered, including explanations of how the board’s current leadership structure benefits shareholders and/or specific factors that may preclude the company from appointing an independent chair.

Overall, it appears that the holistic review has added several new considerations which is likely to make it more difficult for companies to obtain favorable recommendations from ISS. If that is the case, then more independent chair shareholder proposals may pass in the 2015 proxy season, whereas before only a handful have received majority support in prior years.

The FAQs indicate that if a proposal passes, a response short of immediately designating an independent chair may be sufficient at times. A policy that the company will adopt this structure upon the resignation of the current CEO/Chair would be viewed as responsive. Other company actions will be evaluated on a case-by-case basis, depending on the disclosure of shareholder input obtained through the company’s outreach, the board’s disclosed rationale, and the facts and circumstances of the case. It appears that, for example, if a company learns through shareholder engagement that shareholders voted in favor of the proposal because of the absence of a lead director, then it may be enough to appoint one without having to separate the chair and CEO.

The next post will discuss the FAQs on the new equity plan analysis.

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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