

ISS and Glass Lewis Adopt Policy Changes for the 2016 Proxy Season

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Recently, both ISS and Glass Lewis updated their proxy voting guidelines (which are available [here](#) and [here](#)). The ISS updates are effective for meetings on or after February 1, 2016. The following summarizes the major changes of both proxy advisory firms.

Overboarding.

For CEOs of public companies, ISS retained its existing policy of recommending against directors sitting on the boards of more than two public companies besides their own. ISS intends to continue to study the issue and may reconsider it in the future.

For other directors, 2016 serves as a transitional year. ISS will note in its report if a director serves on more than five public company boards, but will only recommend that shareholders vote against directors who sit on more than six public company boards. Starting on or after February 1, 2017, negative recommendations will be made for directors sitting on more than five public company boards.

Beginning in 2017, Glass Lewis will recommend voting against a director (a) who is the executive officer of a public company and sits on more than two public company boards or (b) who serves on more than five public company boards. In 2016, Glass Lewis will note a concern for these directors, thus providing a transition period before putting the full policy into effect.

We note that some major institutional investors have more restrictive overboarding policies. For example, BlackRock may vote against directors who serve on more than four public company boards.

Unilateral Bylaw and Charter Changes.

ISS' current policy already recommends that shareholders vote against directors, committees or the entire board if the board amends the company's bylaws or charter without shareholder approval in a way that "materially diminishes shareholders' rights." A lengthy list of factors it will consider includes the board's rationale, disclosure of engagement with shareholders regarding the amendment and the company's existing governance structure. This policy has now been bifurcated in how it applies to established and newly public companies and the consequences in the years after adoption.

For Existing Public Companies.

ISS notes that it is concerned about an increase in the type of unilateral adoptions, with only 10 in 2013 but 64 in 2014, and so far 62 in 2015. As a result, it is likely to recommend against boards that amended bylaws or charters to (a) classify the board; (b) adopt supermajority vote requirements; or (c) eliminate the shareholder's ability to amend bylaws. In subsequent years, ISS will consider on a case-by-case basis whether to continue recommending against boards unless the amendment is reversed or submitted to a shareholder vote.

For IPO Companies.

ISS will evaluate whether to recommend against directors, committees or boards based on the following:

- the level of impairment of shareholders' rights caused by the provision;
- the company's or the board's rationale for adopting the provision;
- the provision's impact on the ability to change the governance structure in the future (e.g., limitations on shareholder right to amend the bylaws or charter, or supermajority vote requirements to amend the bylaws or charter);

- the ability of shareholders to hold directors accountable through annual director elections, or whether the company has a classified board structure; and
- a public commitment to put the provision to a shareholder vote within three years of the date of the initial public offering.

ISS indicates that in subsequent years unless the adverse provision is reversed or submitted to a vote of public shareholders, it will base its recommendations for directors on a case-by-case basis. Significant weight will be given to shareholders' ability to amend the governance structure in future years through simple majority (not supermajority) vote and boards with annual elections. A public commitment by the company to put the adverse provision to a shareholder vote within three years of the IPO can be a mitigating factor. An IPO company may be able to avoid a negative recommendation by including the commitment in the proxy statements for its first annual meeting.

Exclusive forum provisions (for IPO companies only).

Instead of recommending against the chairman of the nominating and governance committee as it would for an established company, for IPO companies that have adopted exclusive forum, Glass Lewis will evaluate this provision alongside other bylaw terms, such as supermajority vote requirements and a classified board. ISS does not recommend against directors for adopting exclusive forum bylaws.

Proxy Access.

In its survey process, ISS had included questions about specific proxy access bylaw terms. Instead of addressing this in the policy update, ISS will issue an FAQ in December to provide more information on which proxy access provisions ISS considers overly restrictive. The policy update also clarifies the factors ISS will consider in evaluating an actual proxy access nomination and the director candidate, which is substantially similar to the analytical framework it uses for proxy contests.

Glass Lewis has not provided any specific guidelines on proxy access bylaw terms. It continues to use the same analysis for evaluating proxy access shareholder proposals.

Compensation Practices of Externally Managed Issuers (EMIs).

ISS will consider it a problematic pay practice if it believes EMIs have failed to provide sufficient disclosure for shareholders to assess the compensation for named executive officers. EMIs typically do not disclose details about their compensation arrangements or payments made to executives by external managers, which ISS finds troublesome.

Both proxy advisory firms also clarified a number of other policies. Additionally, ISS issued a lengthy FAQ on its equity plan scorecard (which is available [here](#)).

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