



---

An MSCI Brand

---

## 2013 Corporate Governance Policy Updates and Process

### Executive Summary

November 16, 2012

Institutional Shareholder Services Inc.

Copyright © 2012 Institutional Shareholder Services Inc.

[www.issgovernance.com](http://www.issgovernance.com)

## Contents

<b>INTRODUCTION.....</b>	<b>3</b>
<b>SUMMARY OF POLICY UPDATES .....</b>	<b>4</b>
<b>United States Policy Updates .....</b>	<b>4</b>
<b>Canada Policy Updates.....</b>	<b>9</b>
<b>European Policy Updates .....</b>	<b>11</b>
<b>International Policy Updates .....</b>	<b>12</b>
<b>Global Policy Update.....</b>	<b>13</b>
<b>OUTREACH IN 2012 .....</b>	<b>14</b>
<b>Policy Survey.....</b>	<b>14</b>
<b>Policy Roundtables/Client Feedback.....</b>	<b>14</b>
<b>Comment Period .....</b>	<b>14</b>
Summary of Comments .....	14
<b>POLICY FORMULATION PROCESS .....</b>	<b>16</b>
<b>DISCLOSURE/DISCLAIMER .....</b>	<b>17</b>

## INTRODUCTION

Each year, ISS' Global Policy Board conducts a robust and transparent global policy formulation process which culminates in benchmark guidelines to be used in its proxy voting research for the upcoming year. To that end, ISS is pleased to announce its 2013 Global Policy Updates.

The complete set of ISS Global Benchmark Policy Guidelines consider market-specific recommended best practices, transparency, and disclosure when addressing issues such as board structure, director accountability, corporate governance standards, executive compensation, shareholder rights, corporate transactions, and social/environmental issues. The updates contained in this document reflect changes to regional proxy voting policies. These changes are based on significant engagement and outreach with multiple constituents in the corporate governance community, along with a thorough analysis of regional regulatory changes, best practices, voting trends, and academic research.

The 2013 policy updates are grouped by region, including separate documents that specifically address US, Europe, Canada, and International policy changes. Highlights and key changes for the upcoming year include:

- Pay for Performance Evaluation, including peer groups and realizable pay (US)
- Board Responsiveness to Majority Supported Proposals (US)
- Pledging of Company Stock (US)
- Pay for Performance Evaluation, including quantitative and qualitative factors (Canada)
- Voto di Lista (Italy)
- Overboarded Directors (Hong Kong and Singapore)
- Board Tenure (Hong Kong and Singapore)
- Director Nominee Disclosure (Global)

In addition to creating the updates to ISS' Global Policies, the ISS Research team collaborates with over 400 custom clients to ensure that their voting policies reflect their voting philosophy and are updated to take into account trends, practices, and regulatory changes in each market in which they invest.

The full text of the updates, along with detailed results from the Policy Survey, as well as comments received during the open comment period, are all available on ISS' Web site under the [Policy Gateway](#).

The ISS 2013 Global Policy Updates will be effective for meetings on or after February 1, 2013. ISS will release revised Frequently Asked Questions (FAQ) documents in December 2012 that provide additional guidance related to some of the new policies in certain markets.

## SUMMARY OF POLICY UPDATES

The material updates to ISS' benchmark proxy voting policies are summarized below. The full updates, covering U.S., Canada, Europe, and other international markets, are available through the Policy Gateway.

### United States Policy Updates

#### Pay-for-Performance Evaluation

Based on ISS' [2012-2013 Policy Survey](#) results, executive compensation continues to be the perennial top governance topic for investors. Misalignment between pay and performance, problematic pay practices, and board responsiveness are among the key drivers for companies receiving low support on their say-on-pay proposals.

##### *Peer Groups*

ISS' pay for performance evaluation begins with a preliminary quantitative screen of company pay and performance relative to an ISS-selected peer group. For ISS' purposes, these peer groups are designed not for pay benchmarking or stock-picking, but rather to compare pay and company performance within a group of companies that are reasonably similar in terms of industry profile, size, and market capitalization. ISS' current peer group methodology focuses on the subject company's GICS industry classification, which may not reflect multiple business lines in which many companies operate. As a result, some ISS peer groups omitted competitors of the target company and/or included firms that did not reflect a connection to the target considered appropriate for performance and pay comparisons.

The new methodology incorporates information from companies' self-selected pay benchmarking peer groups in order to identify and prioritize GICS industry groups beyond the subject company's own GICS classification. The methodology draws peers from the subject company's GICS group as well as from GICS groups represented in the company's peer group, while maintaining the approximate proportions of these industries in the final peer group where possible. The methodology additionally focuses initially at an 8-digit GICS resolution to identify peers that are more closely related in terms of industry. Finally, when selecting peers, the methodology prioritizes peers that maintain the company near the median of the peer group, are in the subject company's peer group, and that have chosen the subject company as a peer. The peer group methodology maintains its focus on identifying companies that are reasonably similar to the subject company in terms of industry profile, size, and market capitalization.

Other changes to the peer group methodology include using slightly relaxed size requirements, especially at very small and very large companies, and using revenue instead of assets for certain financial companies.

##### *Realizable Pay*

During 2012 proxy season, investors also saw more companies disclosing alternative measures of pay beyond the granted pay disclosed in the summary compensation table. Companies are providing a diverse set of "realizable" total compensation, which endeavors to show how executive pay has been affected by performance. While grant date pay in the Summary Compensation Table shows the intent of the pay decisions of the Compensation Committee, it does not necessarily reflect the final payouts of performance-based awards or changes in value due to gains or losses in the company's stock price.

Based on the ISS' [2012-2013 Policy Survey](#), measures of pay that reflect the company's performance — both standardized calculations and measures of such pay provided by the company — are favored by both issuers and investors as potentially appropriate for consideration in a pay-for-performance evaluation.

Realizable pay is being added to the research report for large capitalization companies. Realizable pay will consist of the sum of relevant cash and equity-based grants and awards made during a specified performance period being measured, based on equity award values for actual earned awards, or target values for ongoing awards, calculated using the stock price at the end of the performance measurement period. Stock options or stock appreciation rights (SARs) will be re-

valued using the remaining term and updated assumptions, as of the performance period, using the Black-Scholes Option Pricing model. The realizable pay consideration may mitigate or exacerbate the CEO's pay for performance concerns.

Overall, the revisions take into account feedback from both investors and issuers based on ISS' [2012-2013 Policy Survey](#) and in-person and telephonic roundtable discussions.

## Board Response to Majority Supported Proposals

The marketplace has been evolving in the matter of board responsiveness to majority-supported shareholder proposals, both in terms of institutional investors' expectations, and in terms of the actual responsiveness by issuers. ISS' [2012-2013 Policy Survey](#) results show that 86 percent of the institutional investor respondents expect that the board should implement a shareholder proposal that receives support from a majority of shares cast in the previous year. Almost half (47 percent) of issuer respondents agreed with that view as well. Issuers have been increasingly responding to shareholder proposals that received only one year of a majority of votes cast: in 2010, 37 percent of the proposals that received only one year of a majority of votes cast in 2009 were implemented (an additional 18 percent received a partial response); in 2012 thus far, 50 percent have been implemented (an additional 6 percent have been partially implemented).

Under the current policy, ISS recommends a vote AGAINST or WITHHOLD from the entire board of directors (except new nominees, who should be considered CASE-BY-CASE) if the board failed to act on a shareholder proposal that received the support of a majority of the shares outstanding in the last year, or a majority of shares cast in the last year and one of the two previous years.

Specifically, the key changes are as follows:

- Include the flexibility to recommend against members of the board as deemed appropriate, not necessarily the full board; and
- Include more guidance on the case-by-case examination of the sufficiency of a company's action in response to a majority-supported shareholder proposal.

In addition, a majority of shares cast at a single meeting will become the trigger to evaluate a company's response to majority-supported shareholder proposals commencing with shareholder proposals appearing on companies' ballots in 2013.

As a result, under this transition rule, the new policy is as follows:

For meetings in 2013, ISS will recommend a vote AGAINST or WITHHOLD from individual directors, committee members, or the entire board of directors as appropriate if:

- the board failed to act on a shareholder proposal that received the support of a majority of the shares outstanding the previous year;
- the board failed to act on a shareholder proposal that received the support of a majority of shares cast in the last year and one of the two previous years.

For meetings in 2014 and thereafter, ISS will recommend a vote AGAINST or WITHHOLD from individual directors, committee members, or the entire board of directors as appropriate if:

- the board failed to act on a shareholder proposal that received the support of a majority of the shares cast in the previous year.

In response to comments received during ISS' 2012 comment period, ISS notes that the application of this policy will be determined on a case-by-case basis. Responding to the shareholder proposal will generally mean either full implementation of the proposal; or, if the matter requires a vote by shareholders, a management proposal on the next annual ballot to implement the proposal. Responses that involve less than full implementation will be considered on a case-by-case basis, taking into account:

- The subject matter of the proposal;
- The level of support and opposition provided to the resolution in past meetings;
- Disclosed outreach efforts by the board to shareholders in the wake of the vote;
- Actions taken by the board in response to its engagement with shareholders;
- The continuation of the underlying issue as a voting item on the ballot (as either shareholder or management proposals); and
- Other factors as appropriate.

ISS will release a revised FAQ document in December 2012 that provides additional guidance related to this new policy.

## Pledging

Pledging of company stock at any amount as collateral for a loan is not a responsible use of equity. Pledging of company stock as collateral for a loan may have detrimental impact on shareholders if the officer is forced to sell company stock, for example, to meet a margin call. The forced sale of significant company stock may negatively impact the company's stock price, and may also violate company insider trading policies. In addition, pledging of shares may be utilized as part of hedging or monetization strategies that would potentially immunize an executive against economic exposure to the company's stock, even while maintaining voting rights.

ISS' [2012-2013 Policy Survey](#) found that 49 percent and 45 percent of institutional and issuer respondents, respectively, indicated that any pledging of shares by executives or directors is significantly problematic. Only 13 percent and 20 percent of institutional investors and issuers, respectively, responded that pledging is not a concern for them. Therefore, both investors and issuers view pledging of company shares as a problematic practice.

ISS' proposed draft policy on the practice of pledging company stock as a problematic pay practice under ISS' say-on-pay evaluation was met with issuer criticism that the draft policy imposes a "one size fits all" approach. Furthermore, based on discussions with several institutional investors on the practice of pledging as a problematic practice, it was indicated that a potential negative vote recommendation should be directed toward the election of directors rather than to a company's say-on-pay proposal. ISS agrees that the practice of significant pledging (as determined to be problematic) may be considered a failure in risk oversight and thus falls under the board's oversight role.

Acknowledging the comments received during ISS' 2012 comment period, ISS will be taking a case-by-case approach in determining whether pledging rises to a level of serious concern for shareholders. Also in response to comments, ISS is including significant pledging of company stock as a failure of risk oversight and thus considered a governance failure whereby directors should be held accountable (rather than communicating concern through a say-on-pay recommendation). In determining vote recommendations for the election of directors at companies who currently have executives or directors pledged company stock, the following factors will be considered:

- Presence in the company's proxy statement of an antipledging policy that prohibits future pledging activity;
- Magnitude of aggregate pledged shares in terms of total common shares outstanding or market value or trading volume;
- Disclosure of progress or lack thereof in reducing the magnitude of aggregate pledged shares over time;
- Disclosure in the proxy statement that stock ownership and holding requirements do not include pledged company stock; and
- Any other relevant factors.

Hedging, on the other hand, is a strategy to offset or reduce the risk of price fluctuations for an asset or equity. Stock-based compensation or open market purchases of company stock are intended to align executives' or directors' interests with shareholders. Therefore, hedging of company stock through covered call, collar, or other derivative transactions severs the ultimate alignment with shareholders' interests. Any amount hedged will be considered a problematic practice warranting a negative voting recommendation on the election of directors.

## Canada Policy Updates

### Pay-For-Performance Evaluation

The current ISS P4P policy is a combination of quantitative and qualitative factors, whereby decision making is largely on a case-by-case basis. However, market perception is often focused on the initial quantitative screen, that is, whether the company underperformed its four-digit GICS group for the prior one- and three-fiscal periods, and CEO compensation increased over the last fiscal year. Issuers and institutional investors have expressed their concern that this "test" is inadequate and potentially misleading. In addition, there has also been concern that the current screening process does not address companies that deliver high pay and pay opportunities in contrast to mediocre performance that marginally exceeds the peer group median. Institutional investors have also indicated that pay-for-performance is the critical factor in determining their votes on management say-on-pay (MSOP) proposals.

The key change is to utilize a new methodology to measure potential long-term pay-for-performance alignment based on the following factors:

#### Quantitative

##### Relative:

1. The Relative Degree of Alignment (RDA) is the difference between the company's TSR rank and the CEO's total pay rank within a peer group<sup>1</sup>, measured over a one-year and three-year period;
2. Multiple of Median (MOM) is the total compensation in the last reported fiscal year relative to the median compensation of the peer group<sup>1</sup>; and

##### Absolute:

3. The CEO pay-to-TSR Alignment (PTA) over the prior five fiscal years, i.e., the difference between absolute pay changes and absolute TSR changes during the prior five-year period (or as long a period as company disclosure permits);

The new methodology generated P4P screen will replace the current P4P screen (TSR below the GICS group median for both one- and three-year periods).

#### Qualitative

Companies identified by the methodology as having potential P4P misalignment will receive a qualitative assessment to determine the ultimate recommendation, considering a range of case-by-case factors. These may include the ratio of performance- to time-based equity awards; the overall ratio of performance-based compensation; the completeness of disclosure and rigor of performance goals; actual results of other financial metrics, special circumstances related to a new CEO in the prior FY; and any other factors deemed relevant.

ISS' [2012-2013 Policy Survey](#) found that size matters in selection of a peer group, when evaluating the alignment between pay and performance in the U.S. market, but also relevant to Canada. Furthermore, institutional investor feedback has further highlighted a need for change in specific aspects of the current ISS policy approach, including: reliance solely on 4-digit GICS peers to evaluate performance (since it is broad and contains companies of varying revenues and market caps) and reliance on a one-year pay change, which emphasizes a short-term trend. The updated P4P evaluation addresses these

---

1. The peer group is generally comprised of 11-24 companies that meet the following criteria:

- Revenue/assets between 0.25X and 4X the subject company's size;
- In the closest GICS industry group (8-digit, 6-digit, 4-digit, or 2-digit) to the subject company's GICS category; and
- Market Cap between 0.25X and 4X of the company's market cap group

In exceptional cases of very large or very small companies, peer groups will be determined on a customized basis.

concerns, while continuing to focus on the CEO's annual pay (including earned pay and incentive grants), since the CEO's compensation "sets the pay pace" at most companies and is directly approved by the compensation committee, which is accountable to shareholders.

Further, granted pay most directly reflects compensation committee decisions about appropriate executive compensation – i.e., the pay that the committee intended to deliver. While prospective incentive grants generally represent pay opportunities that may not be earned or may decline in value in the wake of poor company performance, ISS recognizes that equity-based pay is also highly sensitive to general market trends and may (or may not) deliver significant value regardless of the company's or executive's performance. Investors expect compensation committees to ensure that compensation (including incentive award metrics and goals) follows a pay-for-performance approach. If granted pay is misaligned with actual performance over time, investors want assurance that it is rigorously linked to specific performance improvement.

ISS' view with respect to measuring company performance, particularly supported by client feedback from 2011 roundtable discussions, is that investors ultimately benefit only from the returns on their ownership stake; thus, over time, TSR remains the key performance metric for shareholders. However, ISS' [2012-2013 Policy Survey](#) indicates that a majority (52 percent) of investor respondents would "very likely" consider other metrics in addition to TSR in the U.S. market, but also relevant to Canada. The new methodology continues to evaluate performance on the basis of total shareholder return, while trends in other performance metrics (both absolute and relative) may be considered on a case-by-case basis.

Vote results from 2012 proxy season provide support for ISS' new methodology; although no companies received less than majority support for their MSOP proposals, the companies triggered in the initial testing of the proposed methodology received lower support than the median support for an MSOP proposal in the 2012 proxy season. In Canada, MSOP is not mandatory, and as of Sept. 1, 2012, a total of 106 companies have voluntarily adopted say-on-pay.

## European Policy Updates

### Voto Di Lista (Italy)

In Italy, director elections generally take place through the voto di lista mechanism (similar to slate elections). The Italian implementation of the European Shareholder Rights Directive (SRD) (effective since Nov. 1, 2010) requires that lists of nominees for director and internal auditor elections be published at least 21 days ahead of the meeting (previously 10 days). At the moment, Italian law excludes local banks from the application of the SRD. Currently, there are seven listed local banks in Italy, out of about 270 listed companies.

The new policy acknowledges this disclosure improvement and clarifies that ISS will no longer need to apply an initial negative vote recommendation against director elections, followed by an alert, for companies that fall under the SRD, since disclosure now generally occurs well ahead of custodial voting cutoffs. In addition, the updated policy clarifies ISS' approach in those cases when, for whatever reason, lists of nominees are not disclosed in sufficient time.

Under the current policy, before the lists of director nominees are disclosed, ISS will recommend a vote AGAINST the director elections at such companies. Once the various lists of nominees are disclosed, ISS will issue an alert to its clients and, if appropriate, change its vote recommendation to support one particular slate.

Specifically, the key changes are:

- The publication date for lists would be changed from 10 days before the meeting to 21 days before the meeting for companies that fall under the authority of the SRD; and
- For those companies to which the SRD does not apply (i.e. seven Italian local banks), ISS would continue to issue an initial negative voting recommendation for director elections, followed by a subsequent alert, due to lack of available information at the time the ISS report is published.

Under the new policy, since shareholders only have the option to support one list, where lists are published in sufficient time, ISS will recommend a vote on a CASE-BY-CASE basis, determining which list of nominees it considers is best suited to add value for shareholders based, as applicable, on ISS European policies for Director Elections and for Contested Director Elections.

Those companies that are excluded from the provisions of the European Shareholder Rights Directive publish lists of nominees 10 days before the meeting. In the case where nominees are not published in sufficient time, ISS will recommend a vote AGAINST the director elections before the lists of director nominees are disclosed. Once the various lists of nominees are disclosed, ISS will issue an alert to its clients and, if appropriate, change its vote recommendation to support one particular list.

## International Policy Updates

### Overboarding and Board Tenure (Hong Kong and Singapore)

#### *Overboarding*

In the absence of local laws or best practice code provisions that limit the number of board seats an individual may hold, multiple directorships are currently not considered by ISS when making a director-related vote recommendation in Hong Kong or Singapore. While the average number of board seats held by a director is only 2.2 in Hong Kong and 2.5 in Singapore, a small number of directors in these markets sit on eight or more public company boards; and one director in Hong Kong sits on 16 boards.

With the increasing demands of board and committee service at public companies around the world, investors generally believe that limiting the number of board seats an individual holds is a sensible way to ensure that directors have the time and energy to serve effectively on each board. Some academic studies have confirmed that "busy" directors correlate with lower shareholder returns, while other studies that showed a benefit from adding busy directors to a board – purportedly due to those directors' expertise and network of personal connections – defined "busy" as sitting on three or more boards; well below the threshold for considering a director to be "overboarded" under ISS policies for the U.S., Europe, and Australia.

Under the new policy, which reflects investors' negative sentiment toward overboarded directors, ISS recommends against a director's election where that director sits on a total of more than six public company boards. This policy for Hong Kong and Singapore would more closely align with policies for other developed markets such as the U.S., Europe, and Australia. For 2013, ISS will accept a commitment by an overboarded director to step down from one or more boards at the next annual meeting of the company or companies in question, if that will bring the total number of boards to no more than six.

#### *Board Tenure*

Many investors believe that long tenure on a board can, in some circumstances, lead to a sense of identification with the company and the interests of its management team which can damage a director's independence, even in the absence of a formal transactional or professional relationship between the director and the company. Listing rules in both Hong Kong and Singapore have recently been amended to provide that where a director designated as independent has served on the board for more than nine years, the company should provide the reasons why the board considers such director to still be independent – in effect, creating a rebuttable presumption that independence will be affected by long tenure.

The new policy would classify an "independent non-executive director" as non-independent if such director has served on the board for more than nine years, where the board either fails to provide any reason for considering the director to still be independent, or where the stated reasons raise concerns among investors as to the director's true level of independence. According to ISS' [2012-2013 Policy Survey](#), a majority (55 percent) of investor respondents indicated that in situations where the company provides the reasons why the board considers such director to still be independent, a case-by-case analysis is warranted. ISS plans to evaluate the quality of the disclosure and the reason(s) provided by the company to determine whether a designation of "independent" continues to be appropriate.

## Global Policy Update

### Director Nominee Disclosure

Although most markets provide timely disclosure on the names of director nominees, lack of nominee disclosure remains market practice in several countries, which significantly disenfranchises shareholders voting by proxy. In certain markets, global disclosure practices have noticeably evolved in recent years: in Brazil, the largest market in Latin America, detailed disclosure is now mandatory; and in Europe, the introduction of the EU Shareholder Rights Directive has improved nominee disclosure practices among member states.

According to ISS' 2012-2013 policy survey, more than 76 percent of institutional investors indicated that they would vote against the election of directors at all companies in Latin America, Eastern Europe, and the Middle East/North Africa for failure to disclose nominee names.

ISS is modifying its policies on director nominee disclosure to recommend against the election of directors at all companies if nominee names are not disclosed in a timely manner prior to the meeting. There are two temporary exceptions to this policy:

- Local legislation in Poland allows shareholders to nominate directors up until the date of the general meeting, which has been used to waive the application of the current policy in Poland in the past. However, given the significant improvement in nominee disclosure practices in the EU Member States after the introduction of the EU Shareholder Rights Directive, this lack of disclosure, albeit allowed under local law, shall no longer be acceptable to ISS. Following a one-year grace period during which ISS would include cautionary language in its research reports, the new policy will be fully implemented in Poland in 2014.
- Due to legislative changes published at the end of 2011 in Turkey, companies must now provide the names of independent director candidates prior to their general assemblies. However, most Turkish companies do not provide the names of the remaining (non-independent) candidates. ISS will continue to recommend that shareholders vote against director election proposals at main-index Turkish companies that fail to disclose the names of all board nominees. For non-index Turkish companies, following a one-year grace period during which ISS would include cautionary language in its research reports, the new policy will be fully implemented in 2014.

The updated policy will be better aligned with global best practices and the growing expectations of institutional investors. Furthermore, the proposed one-year grace period would allow non-Index Turkish companies sufficient time to adapt to recent regulatory changes; it would also communicate the upcoming policy change to companies in Poland, where ISS' current policy does not differentiate between index and non-index issuers.

## OUTREACH IN 2012

### Policy Survey

In July, ISS launched the 2012-2013 policy outreach process with our annual policy survey in order to gain a better understanding of the breadth of financial market viewpoints on a range of topics including boards of directors, shareholder rights, and executive compensation. The survey was open to all issuer and investor communities. ISS received responses from 97 institutional investors and 273 corporate issuers.

### Policy Roundtables/Client Feedback

ISS also held various policy roundtables/group discussions on topics that pertain to the U.S., Canadian, and European markets.

For the U.S. market, ISS held four in-person executive compensation roundtable discussions in July and August with investors, issuers, and compensation consultants covering a recap of the 2012 proxy season; pay-for-performance (grant date pay vs. realized/realizable pay); peer groups; non-binding votes on golden parachutes; and say-on-pay frequency for smaller reporting companies.

In September 2012, ISS also held two telephonic roundtable discussions with issuers and investors. One roundtable was on board issues covering: director qualifications and nominating process (for U.S. market); board responsiveness on shareholder proposals that receive one-year majority support of votes cast (for U.S. market); and majority voting (for Canadian market). The other one was on U.S. executive compensation covering: peer group methodology; realized/realizable definition; say on golden parachutes; and pledging of company stock.

Also in September 2012, ISS held three in-person roundtable discussions on European policies with investors on various topics including, but not limited to, approaches to pay; board diversity; related-party transactions; the board's director selection process; and director overboarding.

In addition, ISS held numerous one-on-one and other engagements with clients and issuers in the U.S. and one-on-one engagements with clients in Canada, Europe, and Asia, throughout the year.

### Comment Period

On October 16, ISS invited institutional investors, corporate issuers, and industry constituents to comment on ISS' draft 2013 proxy voting policies.

The comment period, which ran through November 9, produced feedback on eight proposed updates to ISS' global proxy voting policy guidelines. The draft policies on U.S. topics included board responsiveness to majority-supported shareholder proposals, management say-on-pay proposals, say on golden parachute proposals, and proposals calling for the use of environmental and social metrics in executive compensation programs. The key draft policy topic for Canada was pay for performance. In other markets, draft policy topics included director overboarding and board tenure in Hong Kong and Singapore and board nominee disclosure for global markets. ISS received a total of 63 comments (six from investors, 33 from the corporate community, and 24 advisers/consultants or other organizations).

### Summary of Comments

With respect to management say-on-pay proposals in the U.S. market, while most issuers who commented view the proposed peer group selection and realized pay methodologies as improvements, concerns included challenges with identifying peers for larger capitalized companies (holding companies); the use of GICS industry classification; the use of total shareholder returns as a single benchmark; the absence of consensus on what constitutes realizable pay; and mixed views on the use of such realizable pay. Investor respondents did not express significant opposition to ISS' proposed approach to peer group selection, but, as was the case with issuer respondents, there was no consensus on how realizable pay should be defined.

ISS' proposed policy on the practice of pledging company stock was a significant concern to almost all issuers or issuer-related organizations that submitted comments. A common criticism was that the draft policy imposes a "one size fits all" approach in an area not amenable to such an approach and has the potential to indiscriminately penalize the investment decisions of directors and officers. Several issuers suggested that ISS should consider the total amount of stock pledged relative to both the company's total market value and an executive's overall stock holdings, including short and longer term restricted stock and option vesting and ultimately apply a case-by-case approach.

With respect to ISS' draft policy on say on golden parachute proposals to include existing change-in-control arrangements maintained with named executive officers rather than focusing solely on new or extended arrangements, issuers' comments were generally neutral; however, compensation consultants indicated a concern that companies would not be in a position to amend their legacy contractual obligations with executives. ISS notes that the proposed policy continues to be a case-by-case evaluation. Additionally, many companies have amended legacy agreements to eliminate problematic practices in light of shareholder concerns and upon engagement with their investors in many instances.

Comments related to the proposed pay-for-performance methodology for Canada came mostly from issuers or consultants who expressed concerns with ISS' peer selection criteria; the use of realizable pay in the determination of pay and performance alignment; and the use of total shareholder return as the sole metric in the quantitative analysis.

In anticipation of certain challenges involved in selecting relevant peers in the Canadian market, ISS Canada has expanded its peer criteria to ensure that each issuer has relevant and sufficient peer groupings. The quantitative pay for performance evaluation is a screening tool for identifying companies with potential pay for performance misalignments. The ensuing qualitative analysis may take into consideration other factors such as: additional financial metrics, a detailed review of compensation components, rationale on board decisions and methodologies, a comparison of company selected peers, and an assessment of realized vs. granted compensation, in addition to any other factors deemed relevant.

With respect to ISS' proposed policy on board responsiveness in the U.S. market (to hold directors accountable for failure to respond to a shareholder proposal that receives support from a majority of votes cast but not outstanding), while issuers or issuer-related organizations indicated that a case-by-case approach is more appropriate or that a transition period should be provided for the policy to take effect, most investors who commented did not dispute ISS' proposed policy approach.

With respect to proposals calling for the use of environmental and social metrics in executive compensation programs, four comments were received from investors, who indicated general support for modifying ISS' proposed position from a "Generally vote AGAINST" to "Vote Case-By-Case." Given the small number of comments received on these draft policies, ISS notes that they may not be an accurate representation of the viewpoints of the broader shareholder community.

On ISS' proposed policies regarding board nominee disclosure applied to global markets, director overboarding (setting a six board limit), and director tenure (as it impacts director independence) in Hong Kong and Singapore, fewer than five total comments on each proposed policy were received. Of the limited number of comments, investors indicated general support for the idea of voting against director nominees at all companies in all markets if nominee names are not disclosed in a timely manner prior to the company's shareholder meeting. With respect to board tenure, two investors indicated that director tenure is not necessarily correlated with director independence. Given the small number of comments received on these draft policies, ISS notes that they may not be an accurate representation of the viewpoints of the broader shareholder community.

## POLICY FORMULATION PROCESS

The policy review and update process begins with an internal review of emerging issues and notable trends across global markets.

Based on data gathered throughout the year (particularly from client and issuer feedback), ISS forms policy committees by governance topics and markets. As part of this process, the policy team examines academic literature, other empirical research, and relevant commentary. ISS also conducts surveys, convenes roundtable discussions, and posts draft policies for review and comment. Based on this broad input, ISS' Global Policy Board reviews and approves final drafts and policy updates for the following proxy year. Annual updated policies are announced in November and apply to meetings held on and after February 1 of the following year.

Also, as part of the process, ISS collaborates with clients with customized approaches to proxy voting. ISS helps these clients develop and implement policies based on their organizations' specific mandates and requirements. In addition to the ISS regional benchmark (standard research) policies, ISS' research analysts apply more than 400 specific policies, including specialty policies for Socially Responsible Investors, Taft-Hartley funds and managers, and Public Employee Pension Funds, as well as hundreds of fully customized policies that reflect clients' unique corporate governance philosophies. The vote recommendations issued under these policies often differ from those issued under the ISS benchmark policies. ISS estimates that the majority of shares that are voted by ISS' clients fall under ISS' custom or specialty recommendations.

### Key Strengths of ISS ' Policy Formulation Process

*Greater Transparency:* ISS promotes openness and transparency in the formulation of its proxy voting policies and the application of these policies in all global markets. A description of the policy formulation and application process, including specific guidelines and Frequently Asked Questions, appear on our website under the Policy Gateway section.

*Robust Engagement Process with Industry Participants:* Listening to diverse viewpoints is critical to an effective policy formulation and application process. ISS ' analysts routinely interact with company representatives, institutional investors, shareholder proposal proponents, and other parties to gain deeper insight into critical issues. This ongoing dialogue enriches our analysis and informs our recommendations to clients.

*Global Expertise:* ISS ' policy formulation process is rooted in global expertise. ISS ' network of global offices provides access to regional and local market experts for North America, Europe, the Pan-Pacific area, and various emerging markets.

## DISCLOSURE/DISCLAIMER

This document and all of the information contained in it, including without limitation all text, data, graphs, charts (collectively, the "Information") is the property of Institutional Shareholder Services Inc. ("ISS"), its subsidiaries, or in some cases third party suppliers. The Information may not be reproduced or disseminated in whole or in part without prior written permission of ISS.

The Information has not been submitted to, nor received approval from, the United States Securities and Exchange Commission or any other regulatory body. None of the Information constitutes an offer to sell (or a solicitation of an offer to buy), or a promotion or recommendation of, any security, financial product or other investment vehicle or any trading strategy, and ISS does not endorse, approve or otherwise express any opinion regarding any issuer, securities, financial products or instruments or trading strategies.

The user of the Information assumes the entire risk of any use it may make or permit to be made of the Information.

ISS MAKES NO EXPRESS OR IMPLIED WARRANTIES OR REPRESENTATIONS WITH RESPECT TO THE INFORMATION AND EXPRESSLY DISCLAIMS ALL IMPLIED WARRANTIES (INCLUDING, WITHOUT LIMITATION, ANY IMPLIED WARRANTIES OF ORIGINALITY, ACCURACY, TIMELINESS, NON-INFRINGEMENT, COMPLETENESS, MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE) WITH RESPECT TO ANY OF THE INFORMATION.

Without limiting any of the foregoing and to the maximum extent permitted by law, in no event shall ISS have any liability regarding any of the Information for any direct, indirect, special, punitive, consequential (including lost profits), or any other damages even if notified of the possibility of such damages. The foregoing shall not exclude or limit any liability that may not by applicable law be excluded or limited.