2010-2011 Policy Survey Summary of Results

October 26, 2010

Institutional Shareholder Services, Inc.

About the Survey

For the past seven years, ISS has sought feedback on emerging corporate governance issues as a critical component of its annual policy formulation process. ISS seeks input from both its institutional investor clients and the corporate issuer community, in order to get a better understanding of the breadth of financial market views on a range of topics including boards of directors, shareholder rights, and executive compensation/remuneration.

This year's survey was conducted from June 24 through August 9, 2010. ISS' institutional investor clients, as well as a broad global contact list of corporate issuers, were invited to participate in an online survey covering corporate governance developments worldwide. Issuers and investors completed the same survey.

More than 900 total responses were received. A total of 201 institutions responded – approximately 15% of ISS' client base by number. Approximately two-thirds of investor respondents were located in the United States, with the remainder divided between Europe (11%), Canada (7%) and Japan & Australia (2% each). Nearly 700 corporate issuers responded, with 81% of these located in the United States and the remainder divided between Europe (9%), Canada (7%) and Asia-Pacific (3%).

The institutional respondent profile closely follows the overall profile of ISS' clients, with approximately three quarters being asset managers (e.g., investment managers, mutual funds, hedge funds) and the remainder being asset owners (e.g., pension funds, foundations, and endowments). The corporate issuer responses similarly represented a broad range of issuers across the market capitalization spectrum.

Key Findings

Top Governance Issues

Investor respondents focused on the board. Board independence and board competence were identified among the three most important governance topics by a near majority of investors in every region. Risk oversight was also cited by 40 percent or more of investor respondents in all regions. Other important topics mentioned by investors include compensation in Europe and North America and shareholder rights in Asia and developing markets.

Issuers are focusing on risk oversight. For issuers, risk oversight was the most commonly cited topic of importance across all regions, clearly outstripping all other topics (with the exception of executive compensation in North America). Audit-related practices and board competence were also mentioned by a near-majority of issuers in all regions as key issues

Compensation is an American issue. Only for North America (dominated by US respondents) did a majority of issuers (65 percent) cite the perennial issue of executive compensation as one of the top three governance topics for the coming year. In North America, executive compensation also rose to the top of the list for investor respondents, with 60 percent of respondents identifying compensation as one of the three most important issues.

Issuer engagement with ISS is valuable. An overwhelming majority of respondents – both issuers and investors – indicated that it was vital for ISS to engage with issuers across all phases of ISS' research process, from early clarification of issues through issuer "cures" of problematic issues following report publication.

ESG Issues

Environmental, Social and Governance factors are significant. A strong majority of both issuer and investor respondents indicated that ESG factors can have a significant impact on shareholder value in the long term.

Board oversight and shareholder resolutions are the focus. Investors indicated that board oversight of ESG risks and shareholder resolutions promoting greater transparency on ESG issues were the most important factors influencing their proxy voting decision making. For issuers, board oversight was most important. But a large majority of respondents (both issuer and investor) cited ESG factors as important in making proxy voting decisions regarding director competence, compensation, and M&A.

US Board Issues

More pressure for independent board leadership. Three quarters of investor respondents indicated that the head of management (CEO) should not concurrently serve as the head of the board (Chair). While a majority of issuers disagreed, a substantial minority (41 percent) concurred that the two roles should be separate.

When shareholders speak on takeover defenses, boards should listen. Investor respondents indicated that they would not find sufficient a board's halfway implementation of majority-approved shareholder proposals regarding takeover defenses (e.g., declassify board, majority voting, removing supermajority vote provisions, special meeting proposals). A significant majority of issuers, however, embraced board flexibility in responding to this variety of shareholder proposals. The contrast becomes even more stark when looking at boards' unilateral adoption of takeover defenses, with a strong majority of investor respondents (over 80 percent in all case) rejecting unilateral adoption of takeover defenses, and a strong majority of issuer respondents (between 55 and 70 percent) accepting unilateral board action.

US Compensation Practices

Investor and issuer respondents agree: alignment matters. Disclosure of short- and long-term incentives and their relation to business strategy was the factor most commonly cited (approximately 80 percent of each group) as one of the top three in evaluating Say on Pay proposals in the US. The only other factor cited by a majority of investor respondents was non-performance-based pay elements (e.g., perks, tax gross-ups), with pay-for-performance and risk-mitigation cited by approximately 40 percent of investors. For issuers, other commonly mentioned factors include CD&A clarity and company peer groups.

Investors scrutinize incentives. Investor and issuer respondents both overwhelmingly rejected single-trigger change-in-control agreements. Investors reported being lukewarm at best about other change-in-control accelerated vesting provisions, but a majority of investor respondents (55 percent) does accept “double trigger” acceleration provisions. Investors also reported being concerned by a broad range of potentially risk-incentivizing pay practices -- an opinion shared by issuers on a number of particular practices: uncapped bonuses and mega annual equity grants.

Canada

Say on Pay: lever or whip? A majority of both investor and issuer respondents indicated that negative Say on Pay votes should be used infrequently to punish companies in the most egregious cases; however, one third of investors indicated that they would use it as a tool to encourage issuer communications in place of withholding votes from directors. Unsurprisingly, only nine percent of issuers shared that opinion. More than one third of investor respondents also indicated that Say on Pay should be mandated in Canada; conversely, one third of issuers indicated that it should be abolished entirely.

Europe

Pay for performance is most important. A substantial majority of both investors and issuers cited performance criteria and the pay-for-performance link as being among the three biggest concerns in evaluating long-term incentive plans. Also cited was the frequency of awards, with dilution and burn rate mentioned among the top three by 56 percent of investor respondents. Accordingly, an overwhelming majority of investor respondents indicated that pay-for-performance disconnects (increasing compensation with declining performance) could spark a negative vote. And disclosure issues (inconsistent and vague disclosure, especially surrounding performance) also were cited by a majority of investor respondents.

Japan

Expanding scrutiny over independence. A majority of investor respondents reported that additional scrutiny was warranted for companies lacking independent representation on the board of directors – especially those with poison pills (73 percent of investors) and those with majority/controlling shareholders (57 percent).

Appendix: Detailed Survey Responses

Except as otherwise noted, percentages exclude non-responses and any "not applicable" responses.

Critical Governance Principles

What are the top three governance topics in the regions below that are most important to you?

North America	Investors	Issuers
Board independence	53%	31%
Executive compensation	60%	65%
Audit-related practices	12%	29%
Risk oversight	44%	67%
Shareholder rights (special meetings, written consents, amend bylaws)	36%	25%
Takeover defenses	14%	10%
M&A and proxy fights	11%	12%
Environmental/social shareholder proposals	25%	9%
Board competence	49%	49%

Europe	Investors	Issuers
Board independence	59%	29%
Executive compensation	55%	39%
Audit-related practices	14%	41%
Risk oversight	43%	64%
Shareholder rights (special meetings, written consents, amend bylaws)	38%	23%
Takeover defenses	12%	10%
M&A and proxy fights	10%	14%
Environmental/social shareholder proposals	20%	15%
Board competence	55%	53%

Asia-Pacific	Investors	Issuers
Board independence	71%	34%
Executive compensation	31%	30%
Audit-related practices	25%	39%
Risk oversight	37%	68%
Shareholder rights (special meetings, written consents, amend bylaws)	42%	23%
Takeover defenses	20%	15%
M&A and proxy fights	12%	16%
Environmental/social shareholder proposals	19%	9%
Board competence	56%	50%

Developing Markets	Investors	Issuers
Board independence	67%	31%
Executive compensation	29%	25%
Audit-related practices	23%	48%
Risk oversight	40%	73%
Shareholder rights (special meetings, written consents, amend bylaws)	51%	27%
Takeover defenses	10%	9%
M&A and proxy fights	7%	12%
Environmental/social shareholder proposals	17%	13%
Board competence	53%	53%

Engagement

ISS' engagement process comprises the following steps:

A. Prior to delivering the report with vote recommendations, ISS may reach out to issuers to seek clarity on ambiguous issues or lack of disclosure when evaluating a particular proposal, if warranted.
B. During the process of developing a report and vote recommendation on a particular proposal, issuers may reach out to ISS to discuss policy application given the company's specific circumstances.
C. After delivering the report with vote recommendations, issuers may reach out to ISS to provide a "cure" to the underlying issue that triggered an adverse recommendation on a particular proposal or director(s), in order to reverse the recommendation. Such cures generally entail a change, or commitment to change, the problematic practice that resulted in the adverse recommendation.[1]

Do you believe it is vital for ISS to engage with issuers in each of the above phases of the process?

	Investors	Issuers
ISS seeking clarity on ambiguous issues prior to report publication	97%	99%
Issuers providing input on company specifics prior to report publication	90%	97%
Issuers seeking to "cure" issues following report publication	77%	93%

[1] Please note: following delivery of a report, ISS will also work with issuers to the extent a report is shown to be inaccurate. This “correction” process is not considered “engagement” for these purposes.

Poor Disclosure & Tax Havens

Would you generally vote against standard resolutions due to lack of disclosure, even if this would "penalize the market"?

	Investors	Issuers
Yes	56%	30%
No	44%	70%

% of respondents answering yes or no

Should a company that has re-incorporated to a "domicile of convenience," i.e. to reduce its tax burden, be treated as a US-company, provided that (a) It files 10-K annual reports and is not considered a foreign entity by the SEC, (b) Its primary listing is on a US exchange, and not via an ADR program, and (c) Its corporate governance structure is consistent with US practice?

	Investors	Issuers
Yes	85%	86%
No	15%	14%

% of respondents answering yes or no

Related Party Transactions

RPTs with which related parties are of particular concern to you? (Please check all that apply.)

	Investors	Issuers
Directors	93%	90%
Executives	90%	88%
Controlling shareholder	94%	71%
Minority shareholders	42%	19%
Subsidiaries that are not wholly-owned	55%	25%
Sister companies	59%	21%

% of respondents indicating an RPT is of concern.

What types of transactions are of particular concern to you? (Please check all that apply.)

	Investors	Issuers
Agreements to provide financial assistance	85%	60%
Deposit and loan agreements with group financial companies (financing company of the parent)	71%	33%
Loan forgiveness and similar write-offs	90%	67%
Transfer of assets	90%	68%
Severance arrangements	67%	39%
Pension schemes	58%	31%
Consulting or other services	54%	50%

% of respondents indicating a type of transaction is of concern.

Environmental, Social and Governance Issues

Does your organization believe that Environmental, Social and Governance (ESG)factors can have a significant impact on shareholder value in the long term?

	Investors	Issuers
Yes	83%	71%
No	17%	29%

% of respondents answering yes or no

If yes, how important are ESG factors to proxy voting decision-making in the following areas?

Director competence or qualifications

	Investors	Issuers
Very Important	40%	32%
Somewhat Important	44%	36%
Not Important	12%	15%
N/A	4%	17%

Board oversight of exposure to ESG risks

	Investors	Issuers
Very Important	59%	33%
Somewhat Important	38%	46%
Not Important	1%	6%
N/A	2%	16%

Executive or director compensation practices

	Investors	Issuers
Very Important	40%	22%
Somewhat Important	44%	40%
Not Important	12%	21%
N/A	4%	17%

Mergers and acquisitions

	Investors	Issuers
Very Important	32%	22%
Somewhat Important	45%	41%
Not Important	18%	17%
N/A	5%	20%

Supporting shareholder resolutions that promote greater transparency on ESG issues or that encourage comparability of ESG disclosures by corporations

	Investors	Issuers
Very Important	52%	15%
Somewhat Important	33%	41%
Not Important	11%	25%
N/A	3%	19%

United States – Board

Pursuant to new SEC disclosure rules that went into effect in February, companies are required to explain their rationale for appointing a non-independent chair or combing the roles of Chairman and CEO. Should the head of management (CEO) concurrently be the head of the board (Chair) that represents shareholders' interests?

	Investors	Issuers
Yes	24%	59%
No	76%	41%

Under the following scenarios in which a shareholder resolution receives majority support, would you consider the action taken by the board to be sufficiently responsive?

Shareholder Proposal: Adopt majority vote standard for directors

Board Response: Keep plurality standard, adopt director resignation policy

	Investors	Issuers
Not Sufficient	68%	24%
Sufficient	32%	76%

Shareholder Proposal: Declassify the board in one year

Board Response: Phase in declassification over 3 years

	Investors	Issuers
Not Sufficient	36%	13%
Sufficient	64%	87%

Shareholder Proposal: Adopt simple majority vote to amend charter/bylaws

Board Response: Reduce the voting threshold, but keep a supermajority vote requirement (e.g. going from 75% to 66%)

	Investors	Issuers
Not Sufficient	71%	36%
Sufficient	29%	64%

Board Response: Require a majority of shares outstanding (not of shares cast)

	Investors	Issuers
Not Sufficient	55%	12%
Sufficient	45%	88%

Shareholder Proposal: Allow 10% of shareholders to call a special meeting

Board Response: Adopt a higher threshold than 10%

	Investors	Issuers
Not Sufficient	56%	27%
Sufficient	44%	73%

Board Response: Impose agenda restrictions (e.g. no item appearing on annual meeting agenda, such as election of directors)

	Investors	Issuers
Not Sufficient	71%	22%
Sufficient	29%	78%

Board Response: Impose time restrictions on when shareholders can call special meetings (e.g. X days after annual meeting or before the next annual meeting)

	Investors	Issuers
Not Sufficient	45%	11%
Sufficient	55%	89%

Board Response: Require shareholder proponents to pay for the special meeting themselves

	Investors	Issuers
Not Sufficient	75%	21%
Sufficient	25%	79%

United States- Shareholder Rights

Absent any other problematic governance practices at a company, is it appropriate for a board to adopt any of the following takeover defenses unilaterally, i.e. without shareholder approval?

	Investors	Issuers
Classified Board	12%	58%
Super-majority vote requirements to amend bylaws/approve mergers	19%	63%
Eliminate right to act by written consent	12%	63%
Increase the threshold to call special meeting	16%	67%

% of respondents indicating “yes”

United States - Compensation

In the absence of any particular problematic compensation issues, additional information/discussion on which of the topics below is most important in evaluating an advisory vote on executive compensation proposal ("management say on pay")? (Please check the top three only.)

	Investors	Issuers
Disclosure of short-term and long-term incentives and how they relate to the company's business strategy	81%	78%
Pay for performance evaluation under ISS policy	40%	17%
Non-performance-based pay elements (e.g., perks, tax gross-ups, pension plans, CEO service credits for pension plans, deferred compensation balance, above-market interest rate, future CEO base salary)	55%	32%
Company peer group(s) (e.g. list of companies; target benchmarking percentiles)	25%	43%
Employment/Change-in-Control agreements (e.g., trigger, multiple, basis, treatment of equity, excise tax gross-up provision)	26%	23%
Communication (e.g., board responsiveness, prior year MSOP vote, risk assessment)	8%	8%
Risk mitigating practices (e.g., clawback policy, stock ownership, stock retention guidelines)	38%	32%
CD&A clarity/completeness	10%	48%
Internal pay equity (i. e., CEO pay compared to the second-highest paid executive)	10%	8%

As compensation practices (and corresponding ISS benchmark policies) have evolved and boards are more aware of good versus bad compensation practices, should a board be held accountable for past practices even if it commits to eliminate problematic compensation practices in the future?

	Investors	Issuers
Yes	40%	15%
No	60%	85%

Which of the following elements do you believe are acceptable plan provisions for the disposition of awards in the event of a change in control? (Please check all that apply.)

	Investors	Issuers
Accelerated vesting of plan awards with employment termination (i.e., "double-trigger")	55%	85%
Automatic accelerated vesting of all plan awards without employment termination (i.e., "single trigger")	13%	34%
Accelerated vesting of performance shares as if target goals have been met	36%	56%
Accelerated vesting of plan awards if they are not assumed/converted by acquirer	41%	72%
Board discretion to determine award disposition	30%	54%

The following problematic pay practices could potentially incentivize excessive risktaking. Which of these practices would raise concerns sufficient to warrant a shareholder voting response (i.e., against a management say-on-pay resolution or against the compensation committee)? (Please check all that apply.)

	Investors	Issuers
Single performance metric used for short- and long-term plans	63%	40%
High pay opportunities relative to industry peers	62%	35%
Uncapped bonus	66%	56%
Mega annual equity grants that provide unlimited upside with no downside risk	89%	76%
Target long-term multiple that provides standard stock options or time-based equity awards with no performance linkage	71%	30%
Lack of any risk mitigation policies (e.g. companies that do not have clawbacks or anti-hedging policies)	70%	50%

Canada

In light of the compensation practices observed this proxy season in Canada, should management-sponsored "Say on Pay" proposals be? (Please check all that apply.)

	Investors	Issuers
Voted against frequently as just one more tool that provides shareholders with leverage in order to encourage issuer communication regarding compensation concerns, rather than withholding and potentially removing directors under a majority vote policy	33%	9%
Voted against infrequently in only the most egregious cases to punish boards by signaling their failure in overseeing appropriate executive compensation, and may be accompanied by director withholds	56%	56%
Broadened to include director remuneration	35%	16%
Mandated in Canada	35%	7%
Done away with completely	7%	33%

In which of the following scenarios do you consider directors to be independent for purposes of representing minority shareholders on the board and key committees? (Please check all that apply.)

	Investors	Issuers
Voting control (i.e. by means of super-voting shares under a dual class share structure with unequal voting rights) without economic control of more than 50 percent of outstanding equity	36%	20%
Voting control with economic control of more than 50 percent of outstanding equity (i.e. under a one-share-one-vote share structure)	40%	27%
Voting control without economic control of more than 20 percent but less than 50 percent of outstanding equity	60%	70%
Voting control with economic control of more than 20 percent but less than 50 percent of outstanding equity	44%	33%

Europe – Remuneration

What are your three biggest concerns when evaluating long-term incentive plans? (Please choose only three.)

	Investors	Issuers
Dilution/burn rate (i.e. frequency of awards)	56%	39%
Volume reserved for executives	21%	17%
Discount to market	27%	21%
Performance criteria	68%	71%
Pay-for-performance link	48%	67%
Vesting terms	36%	44%
Remuneration committee composition	15%	10%

Other things being equal, which of the following compensation scenarios would raise sufficient concerns to warrant a negative vote? (Please check all that apply.)

	Investors	Issuers
Inconsistent level of disclosure (i.e. some parts of compensation system are disclosed in detail, while others are vague)	75%	44%
No equity-based compensation provided to senior executives	28%	34%
Significant increases to executive remuneration (base or variable) despite long-term negative shareholder returns, recapitalizations, etc.	86%	66%
Performance-oriented variable pay is largely defined on qualitative criteria	50%	28%
Criteria for performance awards are disclosed, but specific targets or potential payout levels are not disclosed	63%	31%
Disclosure of performance metrics is retrospective only	42%	23%
Increase in total remuneration because company performance is strong, despite the current market environment	9%	6%
Move from relative performance measures (e.g. TSR compared to peer group; EPS against inflation) to absolute measures (e.g. absolute TSR growth; share price; absolute EPS figures) in the current market environment	30%	16%

Europe – Director Elections

There are scenarios where policies for board elections may stand in potential conflict with each other. For example, shareholders generally favor majority-independent boards, but also object to poor attendance or excessively long board terms. As such, a shareholder may vote against an independent nominee because of poor attendance or a 6-year term. However, a shareholder vote against this nominee may have the unintended consequence of lowering independence on the board.

In the context above or under a similar scenario, do you believe achieving a majority-independent board is the most important goal in director elections?

	Investors	Issuers
Yes	44%	40%
No	56%	60%

Do you think it is acceptable for individuals who are not members of the board to serve on the nominating committee?

	Investors	Issuers
Yes, and shareholder affiliation of outside members on the committee does not matter.	21%	12%
Yes, but a majority of outside committee members should not represent major shareholders.	26%	12%
No, only directors should serve on the nominating committee.	47%	64%
Other (please specify)	6%	12%

Do you think that annual director (re-) elections should be mandatory?

	Investors	Issuers
Yes	55%	19%
No	45%	81%

Europe – Shareholder Proposals & Director Nominations

Do you think it would be acceptable for a company that currently has a low ownership threshold for submission of a shareholder proposal, to raise its threshold (e.g. from 1 to 3 percent)?

	Investors	Issuers
Yes	50%	63%
No	50%	37%

Japan

Do you approve of deep-discount options that vest before retirement, in order to encourage greater stock ownership by Japanese managers?

	Investors	Issuers
Yes	42%	47%
No	58%	53%

In 2010, many institutional investors voted against representative directors of listed subsidiaries whose boards lack independence. Is similar scrutiny warranted for representative directors at companies with a majority shareholder and/or companies with a poison pill, where the board lacks independence? (Please check all that apply.)

	Investors	Issuers
For companies with a majority shareholder	57%	47%
For companies with a poison pill	73%	37%
Neither	18%	32%

Asia-Pacific ex Japan/Australia/New Zealand

Do you think the lacking sophistication of Asian stock option/performance share schemes should have negative voting consequences?

	Investors	Issuers
Yes	65%	64%
No	35%	29%
Only in some countries	0%	7%

In your mind, what constitutes a "red flag" at Asian companies that should trigger a deeper analysis and possible voting consequences? (Please check all that apply.)

	Investors	Issuers
Resignation of auditors	91%	72%
Resignation of directors	78%	67%
Multiple related party transactions	93%	83%

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