TOWERS WATSON

Jim Kroll
Senior Consultant

875 Third Avenue
New York, NY 10022

T +1 212 725 7550
D +1 212 251 5577
F +1 212 644 7432

james.kroll@towerswatson.com
towerswatson.com

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ISS Global Policy Board

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policy@ISSGovernance.com

ISS Global Policy Board:

On behalf of Towers Watson, I'm submitting the following comments on the ISS draft policy related to the Evaluation of Executive Pay (Management Say on Pay).

Companies continue to enhance their proxy disclosures and explore ways to convey, among other things, how pay is aligned with performance. Appropriate peer groups are the foundation for such an analysis. We understand many companies, and possibly some shareholders, have expressed concerns with current ISS methodology related to pay for performance and the different peer companies used by ISS currently in each component of your analysis.

Our comments below reflect specific recommendations about how ISS defines, applies and communicates about peer groups. In short, we believe it is important for ISS to adopt a transparent methodology for the selection of peers. In addition, we suggest that in light of specific guiding principles, ISS consider the use of company-selected peers in your analysis.

Develop and communicate a set of guiding principles

The draft policy, in adding greater focus on long-term alignment and consistent use of peer companies by ISS for each component of the review, is a logical shift. In undertaking this shift, we believe it will be important for companies to be able to identify the peer companies ISS will use in your evaluation in advance of the publication of the ISS report.

As a matter of policy related to ISS peer group selection, we encourage ISS to communicate "guiding principles" to the marketplace. The development of guiding principles is not meant to influence companies' decisions on who their peers should be. Rather, it will allow companies to prepare thoughtful disclosures that inform shareholders. Given the amount of work companies already devote to peer group selection, we expect the guiding principles will be largely similar to what is currently viewed as a best practice in use by many companies.

Apply the principles against each company's defined peer group

Companies want to use peers that fit them most appropriately and make sense to shareholders. At the same time, companies will want to avoid (to the extent possible) last minute surprises about which companies they'll be judged against under ISS pay-for-performance policies. We understand ISS will want to have some degree of comfort that a company hasn't stacked the deck in its favor by selecting peers that are significantly inconsistent with those that ISS itself would have chosen. Our suggestion offers a compromise approach between these two objectives by allowing a company's self-selected peer group to be used for the ISS pay-for-performance evaluation unless there's a substantial departure (e.g., more than 25%) from the companies that ISS itself would have independently chosen. Where a small percentage of company-selected peers do not overlap the ISS-selected group, ISS would review the company's disclosure related to how and why it chose its peers. ISS could then address any comments related to unique peers in your qualitative review.

Accept the company's group if it generally conforms; if not, address gaps with the principles

Based on our client experience across a broad range of companies, we expect an approach based on mutually understood principles will support a thoughtful process for selecting peer companies. This would allow ISS to base its pay-for-performance analysis on the company-selected peers in many cases. Even where a small percentage of company-selected peers do not overlap with the ISS peers, ISS could become comfortable with a company's process and rationale when reviewing the company's proxy statement and then focus any comments related to the unique company peers in your qualitative review (if other alignment concerns arise).

Should ISS guiding principles and peer selection result in a significant divergence from company peers, ISS could identify situations for closer examination of the company's process and rationale for its peer selection, as described in the company's proxy. This may then lead ISS to use its peers as an independent lens rather than the company peers, along the lines of the draft policy.

This approach would require further consideration initially, but it would encourage an in-depth analysis of the most relevant peers.

Communicate the principles early so that companies could assess their peers relative to the principles

The ability to predict what peers ISS will use aligns with the current ISS practice of transparent policy formation and application. Currently, companies are able to monitor the (TSR) performance component used by ISS based on a quarterly update schedule. We encourage ISS to disclose the detailed peer-selection methodology you will use so that companies can independently estimate the ISS peers with a good deal of certainty. This will allow companies to prepare thoughtful disclosures that inform shareholders, particularly those that may refer to ISS analyses in making decisions about their proxy votes. To do this, companies must be able to identify the peer companies ISS will use in your evaluation well in advance of the release of a company's proxy statement.

A transparent ISS approach is consistent with the detailed processes companies use to select appropriate peers. Such a process, accompanied by meaningful, clear disclosure, can facilitate thoughtful vote decisions and engagement between companies and shareholders.

Thank you again for the opportunity to provide our comments. We welcome any opportunity to discuss our perspective with ISS.

Yours sincerely,

James M Kroll

Jim Kroll
Senior Consultant