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2013-2014 Policy Survey Summary of Results

October 2013

About the Survey

For the past 10 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 July 31, 2013, through Sept. 13, 2013. ISS' institutional investor clients, as well as corporate issuers, were invited to participate in an online survey covering corporate governance developments worldwide. Issuers and investors completed the same survey.

This year, the survey was designed to encourage global market participants to provide regional input on corporate governance issues that are pertinent to all capital markets worldwide. The survey was very concise and structured around several high-level themes including:

- Board responsiveness;
- Director tenure and director rotation;
- Director assessment and role of company performance in director evaluation;
- Equity plan evaluation;
- Share authorizations and issuances; and
- Policy differentiation.

More than 500 total responses were received reflecting more than one response from the same organization. A total of 128 institutional investors responded. Approximately 66 percent of investor respondents were located in the United States, with the remainder divided between U.K., Continental Europe, Canada, and Asia-Pacific**.** 350 corporate issuers responded, 92 percent of which were located in the United States.

Institutions-Category	
Alternative asset management	1%
Custodian bank	3%
Foundation/endowment	3%
Government- or state-sponsored pension fund	15%
Insurance company	1%
Investment manager or asset manager	60%
Investor industry group	1%
Labor union-sponsored pension fund	3%
Mutual fund or mutual fund company	7%
Private bank/wealth management/brokerage	2%
Other	3%

Size of Organization*		
	Institutions	Issuers
Over $100 billion	30%	5%
$10 billion - $100 billion	30%	29%
$1 billion - $10 billion	21%	40%
$500 million - $1 billion	5%	7%
$100 million - $500 million	8%	5%
Under $100 million	3%	1%
Not applicable	3%	14%

*For institutions, size is measured by equity assets under management or assets owned (in U.S. dollars); For issuers, size is measured by market capitalization (in U.S. Dollars)

Market of Focus When Answering Survey Questions		
	Institutions	Issuers
U.S.	46%	80%
Global	34%	15%
Europe	7%	2%
Canada	5%	1%
U.K.	3%	0%
Other	2%	1%
Asia-pacific	1%	0%
Latin America	1%	0%

Key Findings

Board Responsiveness

Survey questions on this topic focused on the issue of board responsiveness to non-binding shareholder mandates in the U.S. market.

Mixed views were elicited on board responsiveness to non-binding shareholder mandates
Investor and issuer respondents diverge on the issue of board responsiveness to non-binding shareholder mandates. Interestingly, responses were also mixed among investor respondents. For investor respondents, 40 percent indicated that the board should be free to exercise its discretion to respond in a manner that it believes is in the best interest of the company and to disclose the rationale for any actions it takes; 36 percent indicated that the board should implement a specific action to address the shareholder mandate; and 24 percent indicated "it depends on the circumstances." Of those that indicated "it depends," responses varied, with most common responses suggesting that it depends on level of shareholder support (or dissent) on the item and the comply-or-explain approach. Of those who indicated the board should implement a specific action to address the shareholder mandate or it depends on the circumstances, a common response among both investor and issuer

respondents suggested that a reasonable time frame for the board to address the mandate is 12-24 months.

On the other hand, 92 percent of issuer respondents indicated that the board should be free to exercise its discretion to respond in a manner that it believes is in the best interest of the company and to disclose the rationale for any actions it takes.

Director Tenure

Survey questions on this topic focused on markets with established corporate governance codes or market practices regarding board member tenure, including the U.K., Continental Europe, and certain markets in Asia.

Investors share concerns over long director tenure
Seventy-four percent of investor respondents indicated that long director tenure is problematic. This percentage includes 15 percent who indicated that lengthy director tenure can diminish a director's ability to serve as an independent steward, 11 percent who indicated that lengthy director tenure can limit a board's opportunities to refresh its membership, and 48 percent who indicated that they share both of those concerns. Only 26 percent of investor respondents indicated that a director's tenure should not be presumed to indicate anything problematic. With respect to issuer respondents, a significant majority (84 percent) indicated that a director's tenure should not be presumed to indicate anything problematic.

With respect to the length of board service that would call into question the independence or continuing service of a board member, the most common response among investor respondents was more than 10 years. While issuer respondents generally indicated that tenure does not hinder director independence or effectiveness, a few expressed that there could be concerns for directors with tenure of more than 15 years.

Regarding the question, "Are there circumstances or situations where a director’s tenure becomes a critical factor when evaluating his or her independence?", a number of investor respondents cited concurrence with the CEO's or other executives' tenures.

Furthermore, 47 percent of investor respondents indicated that an individual's long tenure in board leadership positions (e.g. lead directors, board chairs, chairs of key board committees) raises concern and 25 percent indicated "it depends" on whether long tenure in these positions raises any concerns. Of those who indicated "it depends," other factors to consider include company performance, the company's governance practices, and individual director's strengths. Only 10 percent of issuer respondents agree that a director's long tenure in board leadership positions raises any concern.

Investors and issuers diverge on director rotation
More than one-half of investor respondents indicated that ISS should consider a policy that takes into account director rotation with respect to the board chair (52 percent), lead director (57 percent), or chairs of key board committees (57 percent).

On the other hand, less than 20 percent of issuer respondents would want ISS to consider a director rotation policy with regard to those board positions: board chair (11 percent), lead director (15 percent), or chairs of key board committees (19 percent).

Director Assessment

Survey questions on this topic focused on an assessment of directors in all markets.

Investors and issuers focus on a director's service on other boards
When assessing director performance a significant majority of both investor and issuer respondents agree that a director's current or prior service on the board of other public companies should be a focal point. Issuer respondents (95 percent) tend to focus on positive aspects (e.g. director's breadth of experience) more so than negative aspects (e.g. governance concerns identified regarding the director) as indicated by 70 percent of issuer respondents. On the other hand, 88 percent and 83 percent of investor respondents focus on positive and negative aspects, respectively. Some specific factors to consider when assessing a director's current or prior service on other public company boards, as noted by investor respondents, include director's breadth of experience, relevant expertise to the board or the company's industry, and governance concerns at other public boards. Several issuer respondents shared similar views with those of investors regarding those factors.

Role of Company Performance in Director Evaluation

Survey questions on this topic focused on director evaluation in all markets.

Investors consider company performance in director evaluation with relative TSR cited most frequently as a performance metric
A majority of investor respondents (54 percent) indicated that ISS should always consider company performance when evaluating directors, while 36 percent indicated that ISS should consider company performance when a company has exhibited problematic governance practices that the board does not appear to be addressing.

With respect to performance metrics used to evaluate directors, 91 percent of investor respondents indicated relative total shareholder return and 88 percent indicated financial metrics (e.g. ROE, ROA, ROIC, EPS, margins, economic value change). Of investors who indicated financial metrics, there was no clear consensus on which specific metric is most appropriate, but a common response was that metrics be relevant to the company's industry or sector.

A significant majority of issuer respondents, 74 percent and 79 percent, agree in considering relative TSR and financial metrics, respectively, when evaluating directors. Issuer responses regarding specific financial metrics varied but common responses indicated that metrics should be relevant to the company and its industry. Additional metrics noted by some issuer respondents include cash flow and revenues.

With respect to the time-frame in assessing a board member relative to company performance, the most common response among both investor and issuer respondents was 3-5 years.

Equity-Based Compensation Plans

Survey questions on this topic focused on the evaluation of equity-based compensation plans, primarily in the U.S. market.

Investors significantly weigh performance conditions on awards, cost of equity plans, and other plan features if ISS moves to a holistic approach to equity plan evaluation

Seventy-five percent of investor respondents indicated that performance conditions on awards are "very significant" when weighing factors in a holistic approach to equity plan evaluation, while 64 percent and 57 percent cited cost of plan (e.g. shareholder value transfer cost and/or dilution) and other plan features (e.g. vesting requirements, change-in-control provisions, repricing provisions), respectively, as "very significant." Fifty-seven percent of investor respondents cited plan administration (e.g. burn rate/historical usage of shares, prior history of repricing) as "somewhat significant."

Issuer responses suggest that the above-mentioned factors are not as significant to them when evaluating equity plans in a holistic approach. A majority of issuer respondents, 54 percent, 66 percent, and 61 percent cited cost of plan, other plan features, and plan administration, respectively, as "somewhat significant."

Share Authorizations and Issuances

Survey questions on this topic focused on a number of global markets that require shareholder approval of share issuance authorities and/or of proposed increases to the number of authorized shares. These proposals can be specific (where the purpose and details are disclosed) or general (where it is a nonspecific authority which authorizes future issuances but without an immediate purpose or details that can be evaluated).

Investors care about size of requested authority when voting on general share issuance authorities in conditional capital markets in Europe and Asia

When evaluating proposals seeking general share issuance authorities, i.e. blanket authority with or without preemptive rights, in conditional capital markets in Europe and Asia, all of the factors listed (the size of the requested authority, i.e., potential dilution; the company's historical use of share issuance authorities-track record; duration of authority; and company's governance structure/practices) were important to a significant majority of investor respondents in their voting decisions on these proposals. Specifically, over 75 percent of investor responses indicated each of those factors as important in their voting decisions on these proposals. Of those factors, most investor respondents (93 percent) indicated size of the requested authority.

Historical use of company shares is slightly less important to investors when voting on specific increases to authorized capital in markets such as the U.S.

With respect to proposals seeking specific increases to authorized share capital in markets such as the U.S., all of the factors listed (size of the requested increase; ratio of current shares outstanding compared to new authorization; company's stated use of shares; historical use of company shares; and company's governance structure/practices) were either "very important" or "somewhat important" to a significant majority of investor respondents in their voting decisions on these proposals. Specifically, over 85 percent of investor responses indicated each of those factors as "very important" or "somewhat important" in their voting decisions on these proposals.

Of those factors, size of requested increase, ratio of current shares outstanding compared to new authorization, and company's stated use of shares were most commonly cited as "very important" by most investors, i.e., by 77 percent, 73 percent, and 71 percent of investor respondents, respectively. However, less than one-half (49 percent) of investor respondents indicated that historical use of company shares was "very important" and 43 percent indicated that factor was "somewhat important." More than one-half of investor respondents (54 percent) indicated that a company's governance structure/practices are "very important" in their voting decisions on these proposals.

Differentiation of Policy by Size or Type of Company

Survey questions on this topic focused primarily on European markets where several codes of best practice limit certain portions of their provisions to a select universe of companies, usually delineated according to main index membership.

Investors consider it appropriate for different application of policies on equity compensation provisions based on company size or type

More than one-half of investor respondents (53 percent) indicated that it would be appropriate for ISS to differentiate application of policy on the basis of company size or type when it comes to equity compensation, particularly stock options (i.e. dilution/burn rate). Slightly less than one-half of investor respondents (49 percent) indicated that it would be appropriate with regard to chairman/CEO separation. The affirmative investor response percentages drop to 45 percent on presence of key board committees; 41 percent on requiring a minimum level of independence on the board; and 37 percent on limits of general share issuance authorizations.

On the other hand, a significant majority of issuer respondents, 73 percent, 62 percent, and 58 percent, indicated that differentiating application of policy would be appropriate for equity compensation, chairman/CEO separation, and limits of general share issuance authorizations, respectively.

For those respondents who would find it appropriate to differentiate the application of policy on any of the provisions above, most investor responses (93 percent) as well as issuer responses (93 percent) indicated that a company's size of market capitalization would be an appropriate way of categorizing companies.

Issuers and investors diverge on policy guidelines for small or IPO companies

Regarding differentiating application of policy for smaller or IPO companies, where company disclosure, regulation, or local best practice code permits, there is less appetite among investor respondents for more lenient policy guidelines for small or IPO companies. Just below one-half of investor respondents (49 percent) indicated that ISS should apply the same policy guidelines for all companies. Thirty-two percent of investor respondents indicated that ISS should apply more lenient policy guidelines and only 4 percent indicated that ISS should apply more stringent policy guidelines for smaller or IPO companies.

Of the issuer respondents, a significant majority (67 percent) indicated that ISS should apply more lenient policy guidelines for small or IPO companies.

Of respondents who indicated "it depends" (15 percent of investor respondents; 12 percent of issuer respondents), on whether ISS should differentiate application of policy for smaller or IPO companies, the common and shared responses were that it depends on the policy or governance issue.

Appendix: Detailed Survey Responses

Survey results are based on 151 institutional shareholder responses and 384 issuer responses reflecting more than one response from the same organization.

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

For questions that allowed multiple answers, the percentages will not equal 100 percent. Percentages for certain questions may also not equal 100 percent due to rounding.

Differentiation of Policy by Size or Type of Company

Many good governance practices are designed to ensure a separation of powers and effective protection of minority shareholders. However, some observers note that stringent board independence requirements, capital issuance restrictions, and some other governance recommendations may be inappropriately onerous for smaller or other types of companies. This is recognized by several European codes of best practice which limit certain portions of their provisions to a select universe of companies, usually delineated according to main index membership; while some markets apply different rules to companies based on size or listing segment. In recognition of this, several provisions in ISS' policies distinguish between companies of different sizes, based either on membership of the market's main index or size of market capitalization.

In your view, would you consider it appropriate for ISS to differentiate application of policy on the basis of company size or type on any of the following provisions?

% of Respondents Answered Yes	Institution	Issuer
Chairman/CEO separation	49%	62%
Provisions requiring a minimum level of independence on the board	41%	47%
Presence of key board committees	45%	52%
Limits of general share issuance authorizations	37%	58%
Equity compensation, particularly stock options (i.e. dilution/burn rate)	53%	73%

If you answered yes to any of the provisions above, which of the following ways of categorizing companies would you consider could be appropriate?

% of Respondents Answered Yes	Institution	Issuer
Size of market capitalization	93%	93%
Index membership	37%	36%
Where disclosure and other regulatory requirements differ	76%	81%
Recent IPOs (e.g., within last 2 years)	59%	64%
Where local codes of best practice make the differentiation	70%	58%

Company disclosure, regulation or local best practice code permitting, would you want ISS to differentiate application of policy for smaller or IPO companies?

	Institution	Issuer
Yes – ISS should apply more lenient policy guidelines	32%	67%
Yes – ISS should apply more stringent policy guidelines	4%	1%
No – ISS should apply the same policy guidelines for all companies	49%	20%
It depends	15%	12%

Board Responsiveness

In some markets, all voting items are binding (i.e. the board must implement an item that receives a majority vote from shareholders), whereas in other markets, some votes are advisory in nature whereby board discretion is applied. When evaluating directors, institutional investors may, for example in the U.S. market, consider the level of board responsiveness to a majority shareholder vote on nonbinding shareholder proposals or a high level of dissent on advisory say-on-pay resolutions or director elections.

Where a board is not required to take action in response to a shareholder mandate, what approach should be used in evaluating board responsiveness?

	Institution	Issuer
The board should be free to exercise its discretion to respond in a manner that it believes is in the best interest of the company and to disclose the rationale for any actions it takes.	40%	92%
The board should implement a specific action to address the shareholder mandate.	36%	3%
It depends on the circumstances	24%	5%

Director Assessment

When assessing director performance, what is your focus when considering a director's current or prior service on boards of other public companies?

% of Respondents Answered Yes	Institution	Issuer
We focus on positive aspects (e.g. director's breadth of experience)	88%	95%
We focus on negative aspects (e.g. governance concerns identified regarding the director)	83%	70%

Director Tenure

Some markets have developed policies and standards regarding board member tenure. In other markets, board tenure is a topic that generates debate, but not broad consensus. In line with best practice codes or listing requirements, tenure impacts ISS' independence classification of directors in a number of global markets. For example, in most of continental Europe, a director with tenure exceeding 12 years is deemed non-independent. In the United Kingdom, Ireland, Italy, Hong Kong and Singapore, directors with a tenure exceeding nine years are considered non-independent, unless the company provides sufficient and clear justification that the director is independent despite his/her long tenure.

Do you believe that long director tenure is problematic?

	Institution	Issuer
Yes – A director's ability to serve as an independent steward is diminished when he or she has served too long.	15%	3%
Yes - Lengthy director tenure limits a board's opportunities to refresh its membership.	11%	6%
Yes – I share both of the concerns listed above.	48%	8%
No – A director's tenure should not be presumed to indicate anything problematic.	26%	84%

Few, if any, markets have best practice guidelines addressing the tenure of lead directors, board chairs, and/or chairs of key board committees (e.g., audit, compensation, nominating committee). Do you believe that an individual director's long tenure in these positions raises any concerns?

	Institution	Issuer
Yes	47%	10%
No	28%	68%
It depends	25%	22%

Should ISS consider a policy that takes into account director rotation with regards to the board chair, lead director, or chairs of key board committees?

% of Respondents Answered Yes	Institution	Issuer
Board chair	52%	11%
Lead director	57%	15%
Chairs of key board committees	57%	19%

Role of Company Performance in Director Evaluation

Some investors consider a company's financial performance when evaluating board members. ISS' voting policies for board elections in some markets apply performance screens. In the U.S. market, for example, ISS applies a Director Performance Evaluation policy that considers relative TSR performance in conjunction with other governance factors when evaluating director elections.

In what situation should ISS consider a company's performance when evaluating directors?

	Institution	Issuer
ISS should always consider company performance.	54%	25%
ISS should consider company performance when a company has exhibited problematic governance practices that the board does not appear to be addressing.	36%	49%
ISS should never consider company performance.	2%	13%
Performance should be considered in the following instances	8%	12%

If you chose an answer above other than "ISS should never consider company performance," would you consider the following performance metrics?

% of Respondents Answered Yes	Institution	Issuer
Relative Total Shareholder Return (share price appreciation plus dividend payouts)	91%	74%
Financial metrics (e.g. ROE, ROA, ROIC, EPS, margins, economic value change)	88%	79%

Equity-Based Compensation Plans

ISS applies a case-by-case approach on equity based compensation plans, generally recommending a vote against plans for high cost/dilution (a key factor), problematic features, lack of compliance on best practices in certain markets, among others. Any of these factors can independently lead to a recommendation against the plan, and factors do not balance against one another. For example, a plan's low potential cost would not mitigate a high average burn rate at the company. Additionally, potentially beneficial features such as robust vesting requirements in plan documents, a requirement for performance conditions on awards, double- trigger acceleration upon a change in control do not outweigh negative features in the evaluation of a plan.

If ISS moves to a more holistic approach to equity plan evaluation, please indicate how significantly you would weigh the following factors (whether positively or negatively):

Institutional Shareholder Respondents:

Factor	Very Significant	Somewhat Significant	Not Significant
Cost of plan (e.g., Shareholder Value Transfer Cost and/or dilution)	64%	33%	3%
Performance conditions on awards	75%	20%	4%
Other plan features (e.g. vesting requirements, change-in-control provisions, repricing provisions)	57%	40%	2%
Plan administration (e.g. burn rate/historical usage of shares, prior history of repricing)	39%	57%	5%
Company's long-term TSR relative to peers	42%	45%	13%

Issuer Respondents:

Factor	Very Significant	Somewhat Significant	Not Significant
Cost of plan (e.g., Shareholder Value Transfer Cost and/or dilution)	38%	54%	9%
Performance conditions on awards	28%	48%	24%
Other plan features (e.g. vesting requirements, change-in-control provisions, repricing provisions)	22%	66%	12%
Plan administration (e.g. burn rate/historical usage of shares, prior history of repricing)	25%	61%	14%
Company's long-term TSR relative to peers	19%	42%	39%

Share Authorizations and Issuances

A number of global markets require shareholder approval of share issuance authorities and/or of proposed increases to the number of authorized shares. These proposals can be specific (where the purpose and details are disclosed, and therefore a case-by-case evaluation can be provided) or general (where it is a nonspecific authority which authorizes future issuances but without an immediate purpose or details that can be evaluated). Such votes may provide investors with a means of checking a board's use of equity capital and minimizing potential dilution, but general authorities in particular can carry concerns for shareholders.

In evaluating proposals seeking general share issuance authorities (i.e. blanket authority with or without preemptive rights) in conditional capital markets* in Europe and Asia, are the following factors important in your voting decision?

% of Respondents answering Yes	Institution	Issuer**
Size of the requested authority, usually expressed as a proportion of current share capital (i.e. potential dilution)	93%	85%
The company's historical use of share issuance authorities (track record)	83%	78%
Duration of authority	77%	63%
Company's governance structure/practices	81%	73%

*Under the conditional capital system, companies seek authorization for pools of capital with fixed periods of availability. For example, if a company seeks to establish a pool of capital for general issuance purposes, it requests the creation of a certain number of shares with or without preemptive rights, issuable piecemeal at the discretion of the board for a fixed period of time. Shares unissued after the fixed time period lapse.

**Issuer percentages are based on 60 responses for each of the factors, respectively, in the table above. Either 223 or 224 issuer responses indicated "Not applicable (my organization does not vote)" for each of the factors, respectively, which are excluded from the response count.

With respect to proposals seeking specific increases to authorized share capital in markets such as the U.S., how important are the following factors in your voting decision?

Institutional Shareholder Respondents:

Factor	Very Important	Somewhat Important	Not Important
Size of the requested increase	77%	20%	4%
Ratio of current shares outstanding compared to new authorization	73%	22%	4%
Company's stated use of shares	71%	27%	2%
Historical use of company shares	49%	43%	8%
Company's governance structure/practices	54%	33%	13%

Issuer Respondents*:

Factor	Very Important	Somewhat Important	Not Important
Size of the requested increase	48%	43%	9%
Ratio of current shares outstanding compared to new authorization	50%	41%	9%
Company's stated use of shares	44%	44%	12%
Historical use of company shares	30%	49%	21%
Company's governance structure/practices	29%	47%	24%

* Percentages are based on range of responses between 127 and 129 for each factor, respectively, in the table above. Between 170 and 173 issuer responses indicated "Not applicable (my organization does not vote)" for each of the factors, respectively, which are excluded from the response count.