US Policy - Director Elections - Non-Employee Director Compensation

Background and Overview

Non-employee director (NED) compensation has come into the corporate governance spotlight in recent years. ISS' 2017 Board Practices Study indicated that median NED pay at S&P 1500 firms has steadily increased every year since 2012 and stood at approximately $211,000 in 2016. As director pay has risen, investors have shown a growing interest in the magnitude of boardroom compensation and the structure of pay packages. Some investors have gone a step further by challenging director pay in proxy contests and legal actions. Many companies have responded to this pressure and unfavorable judicial rulings by adding annual compensation limits to their director equity award program or introducing proposals that seek shareholder approval of the director compensation program.

Although NED pay magnitude varies by company size and industry, ISS has identified some extreme pay outliers - the reasons for which are sometimes not clearly explained by companies. Investor respondents to ISS' 2018 Policy Application Survey indicated a strong preference for adverse vote recommendations where a pattern of excessive NED pay levels at a company has been identified. The least-favored action advocated by investor respondents to the survey was making no adverse vote recommendations.

Currently, NED compensation is broadly addressed under ISS' five Compensation Global Principles. The fifth principle states that companies should avoid inappropriate pay for non-employee directors.

Key Changes Under Consideration

The proposed new policy would explicitly provide for adverse vote recommendations for board committee members who are responsible for approving/setting NED compensation when there is a pattern (i.e. two or more consecutive years) of excessive NED pay magnitude without a compelling rationale or other mitigating factors.

Intent and Impact

This proposed policy seeks to hold accountable directors who approve excessive NED pay without a compelling rationale or other justification.

There would be no impact on vote recommendations in 2018 for directors as a result of this proposed policy. Going forward, negative recommendations would be triggered only after a pattern of excessive NED pay is identified in consecutive years. ISS expects a minimal impact for boards as the policy is focused on extreme director pay outliers.

Request for Comment

While we appreciate any comments on this topic, ISS is specifically seeking feedback on the following:

- In your view, what are the circumstances for which large NED pay magnitude would merit support on an exceptional basis (e.g., one-time onboarding grants to new directors)?
- If a company's proxy disclosure does not clearly indicate which board committee is responsible for setting and/or approving director pay, which board members should be held accountable?
- In calculating average/median pay, should ISS include outsized pay packages provided to NED board chairs, lead directors or other board members who receive outsized boardroom pay?