



United States

Public Fund Proxy Voting Guidelines Updates

2017 Policy Recommendations

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BOARD OF DIRECTORS- VOTING ON DIRECTOR NOMINEES IN UNCONTESTED ELECTIONS

Restricting Binding Shareholder Proposals

▶ **Current Public Fund Advisory Services Recommendation:** None

Key Changes:

- › Adoption of a new policy under Director Accountability where shareholders do not have the ability to amend the bylaws.

▶ **New Public Fund Advisory Services Recommendation:** Generally vote against or withhold from members of the governance committee if:

The company's charter imposes undue restrictions on shareholders' ability to amend the bylaws. Such restrictions include, but are not limited to: outright prohibition on the submission of binding shareholder proposals, or share ownership requirements or time holding requirements in excess of SEC Rule 14a-8. Vote against on an ongoing basis.

Rationale for Update:

Shareholders' ability to amend the bylaws is a fundamental right. Under SEC Rule 14a-8, shareholders who have held shares valued at \$2,000 or more for one year are permitted to submit shareholder proposals, both precatory and binding, to amend the bylaws. Some states permit companies to restrict this right in their charters. These prohibitions amount to a material diminution of shareholder rights. Although some companies have offered management proposals as alternatives, these often have greater ownership or holding period requirements and have typically not been well received by the shareholders of non-controlled companies.

Client feedback indicates that these prohibitions flew under the radar until relatively recently. Over the last several years, shareholders have submitted precatory proposals seeking the right to amend the bylaws at a number of companies that do not provide this right to shareholders. A number of these campaigns were contentious and generated interest on the topic among members of the wider investor community.

Unilateral Bylaw/Charter Amendments - IPO Companies


▶ **Current Public Fund Advisory Services Recommendation:** For newly public companies, generally vote against or withhold from directors individually, committee members, or the entire board (except new nominees, who should be considered case-by-case) if, prior to or in connection with the company's public offering, the company or its board adopted bylaw or charter provisions materially adverse to shareholder rights, considering the following factors:

- › The level of impairment of shareholders' rights caused by the provision;
- › The disclosed rationale for adopting the provision;
- › The ability to change the governance structure in the future (e.g., limitations on shareholders' right to amend the bylaws or charter, or supermajority vote requirements to amend the bylaws or charter);
- › The ability of shareholders to hold directors accountable through annual director elections, or whether the company has a classified board structure; and,
- › A public commitment to put the provision to a shareholder vote within three years of the date of the initial public offering.

Unless the adverse provision is reversed or submitted to a vote of public shareholders, vote case-by-case on director nominees in subsequent years.

Key Changes:

- › The heading will be amended to read: Unilateral Bylaw/Charter Amendments and Problematic Capital Structures;
- › Adverse vote recommendations for director nominees will generally be warranted if a company completes its public offering with a multi-class capital structure in which the classes do not have identical voting rights;
- › A vote by shareholders within 3 years will be insufficient; a sunset provision will be necessary.

 **New Public Fund Advisory Services Recommendation:** For newly public companies, generally vote against or withhold from directors individually, committee members, or the entire board (except new nominees, who should be considered case-by-case) if, prior to or in connection with the company's public offering, the company or its board adopted bylaw or charter provisions materially adverse to shareholder rights, or implemented a multi-class capital structure in which the classes have unequal voting rights considering the following factors:

- › The level of impairment of shareholders' rights;
- › The disclosed rationale;
- › The ability to change the governance structure (e.g., limitations on shareholders' right to amend the bylaws or charter, or supermajority vote requirements to amend the bylaws or charter);
- › The ability of shareholders to hold directors accountable through annual director elections, or whether the company has a classified board structure;
- › Any reasonable sunset provision; and
- › Other relevant factors.

Unless the adverse provision and/or problematic capital structure is reversed or removed, vote case-by-case on director nominees in subsequent years.

Rationale for Update:

There has been an increase in the number of companies completing initial public offerings with multi-class capital structures:

Year	# of IPO companies with multi-class structures
2006	8
2007	6
2008	9
2009	2
2010	4
2011	6
2012	11
2013	12
2014	21
2015	18
2016 (as of Aug. 30)	17

The 2016 – 2017 policy survey results indicate that a majority of investor respondents are in favor of issuing adverse vote recommendations for director nominees when a company completes its initial public offering with a multi-class structure or a multi-class structure with no sunset provision for unequal voting rights.


CAPITAL

Stock Distributions: Splits and Dividends

 **Current Public Fund Advisory Services Recommendation:** None

Key Change:

› Include a specific policy on stock splits and dividends in the policy guidelines.

 **New Public Fund Advisory Services Recommendation:** Generally vote for management proposals to increase the common share authorization for stock split or stock dividend, provided that the increase in authorized shares is reasonable in accordance with Public Fund Advisory Services' Common Stock Authorization policy.

Rationale for Update:

A policy as it pertains to forward stock splits and stock dividends is relevant because proposals to increase authorized common shares may be tied to the implementation of a planned stock split or stock dividend. Forward stock splits may have the effect of enhancing the liquidity of the company's shares. Companies often use stock splits to attract potential investors, as they tend to increase the stock's marketability by increasing the public float and bringing the market price more in line with the average investor's ability to purchase a round lot.

DIRECTOR COMPENSATION

Shareholder Ratification of Director Pay Programs

▶ **Current Public Fund Advisory Services Recommendation:** None

Key Changes:

- › Codify the evaluation framework applied to newly-seen U.S. ratification of non-employee director pay programs.

▶ **New Public Fund Advisory Services Recommendation:** Vote case-by-case on management proposals seeking ratification of non-employee director compensation, based on the following factors:

- › If the equity plan under which non-employee director grants are made is on the ballot, whether or not it warrants support; and
- › An assessment of the following qualitative factors:
 - › The relative magnitude of director compensation as compared to companies of a similar profile;
 - › The presence of problematic pay practices relating to director compensation;
 - › Director stock ownership guidelines and holding requirements;
 - › Equity award vesting schedules;
 - › The mix of cash and equity-based compensation;
 - › Meaningful limits on director compensation;
 - › The availability of retirement benefits or perquisites; and
 - › The quality of disclosure surrounding director compensation.

Rationale for Update:

There have been a number of recent high profile lawsuits regarding excessive non-employee director ("NED") compensation that reflect increasing shareholder scrutiny on the topic. In response, some companies have put forth advisory proposals seeking shareholder ratification of their NED pay programs. Public Fund Advisory Services evaluated several director pay proposals during the 2016 proxy season, and we expect to see more submitted to a shareholder vote. Accordingly, a policy framework to evaluate such proposals is necessary.

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