Executive Summary

Proxy Voting Guideline Updates and Process

2017 Benchmark Policy Recommendations

Effective for Meetings on or after February 1, 2017

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SUMMARY OF ISS' POLICY FORMULATION PROCESS

Each year, ISS' Global Policy Board conducts a robust, inclusive, and transparent global policy formulation process that produces the ISS benchmark proxy voting guidelines that will be used during the upcoming year.

The policy review and update process begins with an internal review of emerging issues and notable trends across global markets. Based on information gathered throughout the year (particularly from investor and issuer feedback during proxy season), ISS forms policy committees to examine various governance topics in specific global markets. As part of this process, the policy team examines relevant academic research, other empirical studies, and commentary by market participants. ISS also conducts surveys, convenes roundtable discussions, and posts draft policies for a review and comment period. Based on this broad input, ISS' Global Policy Board reviews and approves final policy updates for the following proxy year. Updated policies announced in November of each year apply to meetings held on and after February 1 of the following year.

As part of the annual review process, ISS also works with clients who utilize customized approaches to proxy voting. ISS helps these clients to develop and implement policies based on their organizations' specific mandates and requirements. In addition to the ISS regional Benchmark (standard research) policies, ISS' research analysts apply more than 400 specific policies that reflect clients' unique corporate governance philosophies and investment strategies. The customized solutions also include specialty policies for Socially Responsible Investors, Taft-Hartley funds and their external asset managers, and Public Employee Pension Funds. The vote recommendations issued under these policies often differ from those issued under the ISS benchmark policies. The majority of shares that are voted by ISS' clients via ISS' voting platform fall under ISS' custom or specialty recommendations.

Key Strengths of the ISS Policy Formulation Process

Industry-Leading Transparency: ISS promotes openness and transparency in the formulation of its proxy voting policies and the application of these policies in all global markets. A description of the policy formulation and application process, including specific guidelines and Frequently Asked Questions, appears on our website under the Policy Gateway section.

Robust Engagement with Industry Constituents: Listening to diverse viewpoints is critical to an effective policy formulation and application process. ISS' analysts routinely interact with institutional investors, company representatives, shareholder proposal proponents, board members, and other parties to gain deeper insight into critical issues. This ongoing dialogue enriches our analysis and informs our recommendations to clients.

Global Expertise: ISS' policy formulation process is rooted in global expertise. ISS' network of global offices provides access to regional and local market experts for the Americas, EMEA (Europe/Middle East/Africa), and Asia-Pacific regions.

2016-2017 Outreach

Policy Survey

In August 2016, ISS launched the 2016-2017 policy outreach cycle with our annual policy survey. The survey encouraged global market participants to provide input on corporate governance issues that are pertinent to capital markets worldwide. This year's survey covered topics including overboarding; dual-class capital structures at IPO companies; shareholders' inability to amend company bylaws; non-executive director compensation programs; the metrics used in pay-for-performance assessments; the frequency of say-on-pay votes; the alignment of compensation/remuneration-related votes at cross-market companies; and board composition/director independence in Asian and Latin American markets. The survey was open to the entire issuer and investor communities and ISS also solicited input from a broad range of other governance stakeholders. ISS received responses from 120 institutional investors and 299 members of the corporate issuer community (including corporate issuers, consultants/advisers to issuers, and other organizations representing issuers). Additional responses were received from investor coalitions, NGOs and academics. Responses came from the US, Europe, Canada and the Asia-Pacific region.

Policy Roundtables/Feedback

ISS also held various policy roundtables/group discussions on topics that pertain to the U.S., Canadian, European, and Asia-Pacific markets.

For the U.S. market, ISS held three roundtable discussions with various market constituents as follows:

- On Sept. 19, 2016, an in-person roundtable in New York City with institutional investors discussed enhancements to ISS's pay-for-performance quantitative screen, say-on-pay frequency, non-employee director pay, overboarding for executive chairs, and board tenure/refreshment.
- On Oct. 6, a telephonic roundtable with institutional investors, a corporate director and a compensation consultant covered enhancements to the pay-for-performance quantitative screen, termination-related compensation arrangements, compensation proposals at cross-market companies, and non-employee director pay.
- On Oct. 17, a telephonic roundtable with institutional investors and directors covered sunset provisions for IPO governance structures, share issuance mandates at foreign-incorporated, US-listed companies, and overboarding by executive chairmen.

For the Canadian market, ISS held a roundtable discussion on Sept. 29 with institutional investors, which covered executive chair overboarding, subsidiary boards and overboarding, cooling-off periods for related party transactions/professional services, non-employee director inducement grants, and the basis for burn rate calculations for PSUs and performance stock options.

In Europe, three separate in-person roundtable discussions were held with institutional investors in September.

- ISS held policy roundtable discussions with institutional investors in Edinburgh and London on Sept. 8 and 13, covering the EMEA pay-for-performance model, director overboarding and executive remuneration in the UK, among other topics.
- On Sept. 15, 2016, ISS held a policy roundtable discussion with institutional investors in Paris covering the EMEA pay-for-performance model, issues surrounding director overboarding, executive pay in the French market, and the separate functions of CEOs and board chairs, among other topics.

For Asia-Pacific markets, ISS held roundtable discussions with institutional investors on Sept. 27 in Hong Kong and on Sept. 29 in Singapore. Discussion topics included dividend proposals in China that carry tax implications for investors when conducted through bonus share issuances via capitalization of retained earnings, the introduction of independence criteria for director elections in Taiwan, lead independent directors in Singapore, and overboarding in India. In Japan, in lieu of roundtable discussions, one-on-one meetings were held with nine institutional investors in July and August to discuss the appointment of advisors, the board-with-audit-committee governance structure, ROE policy, dividend policy, compensation, takeover defenses and company disclosure practices related to board independence.

In addition, ISS held numerous one-on-one and other discussions throughout the year with institutional investors, issuers, and other stakeholders in the U.S., Canada, Brazil, Europe, Australia, Japan and Asia ex-Japan.

Comment Period

On Oct. 27, ISS invited institutional investors, corporate issuers, and industry constituents to comment on ISS' draft 2017 proxy voting policies on select topics. The comment period, which ran through Nov. 10, sought feedback on 15 proposed updates to ISS' global proxy voting policy guidelines. The draft policy updates on U.S. topics included IPOs with multi-class capital structures, shareholders' inability to amend company bylaws, and general share issuance mandates for US-listed cross-market companies. For Canada, feedback was sought on compensation for non-executive directors. For Europe, feedback was sought on policy updates related to overboarding, non-executive director remuneration, committee composition at smaller companies in the UK and Ireland, and ISS's European pay-for-performance methodology. For Asia-Pacific markets, the topics included the creation of advisory positions for former executives in Japan and various board-related topics in Taiwan and South Asian markets. Feedback was also sought on the topics of board independence in Brazil and other Latin American markets, and the appropriate policy approach for executive pay assessments at cross-market companies.

ISS received a total of 46 comments: six from institutional investors or investor groups, nine from law firms, one from a compensation consultant, one from a business organization, and the remainder from the corporate issuer community. A summary of the comments is included in the Appendix.

South Africa Policy Update

In September 2016, ISS updated the South Africa policy guidelines, for meetings on or after Oct. 1, 2016. Whereas the previous policy evaluated director attendance only at meetings of the full board, the updated policy takes account of director attendance at meetings of the key committees (audit, nomination and remuneration) on which those directors serve, on an aggregated basis with attendance at meetings of the full board.

Upcoming Milestones

December 2016:

- ISS will release a complete set of updated policies (in full and/or summary form).
- ISS will release updated Frequently Asked Questions ("FAQ") documents on certain U.S. policies.

January-February 2017:

- *January:* ISS will evaluate new U.S. shareholder proposals anticipated for 2017 and update its U.S. Summary Proxy Voting Guidelines accordingly.
- *February 1*: 2017 Global Policy Updates will take effect for meetings that occur on or after this date.

SUMMARY OF POLICY UPDATES

ISS's Global Benchmark Policy Guidelines consider market-specific regulation and best practices, transparency, and direct input from institutional investor clients and other market constituents in addressing issues such as board structure, director accountability, corporate governance standards, executive compensation, shareholder rights, corporate transactions, and social/environmental issues. The updates contained in this document reflect changes to proxy voting policies within ISS's three research regions – the Americas, EMEA (Europe/Middle East/Africa), and Asia-Pacific. These changes are based on significant engagement and outreach with multiple constituents in the corporate governance community, along with a thorough analysis of regulatory changes, best practices, voting trends, and academic research.

The 2017 policy updates are grouped by region with separate documents addressing Americas, EMEA, and Asia-Pacific policy changes. The full updates are available through the Policy Gateway. Policies being amended for the upcoming year include:

- Overboarding (Continental Europe, UK/Ireland, India, Hong Kong, Taiwan)
- Equity Plan Scorecard updates (U.S.)
- Executive compensation (Continental Europe, UK/Ireland; cross-market)
- Non-employee director compensation (U.S., Canada, Continental Europe)
- IPOs with dual-class capital structures (U.S.)
- Shareholder inability to amend bylaws (U.S.)
- Permitted bid periods for shareholder rights plans (Canada)
- Creation of advisory posts for former executives (Japan)
- Board independence (Continental Europe, Canada, Latin America, Taiwan)
- Committee independence (UK/Ireland)
- Director attendance (Pakistan, Bangladesh, Sri Lanka, Taiwan)

The full text of the updates, along with detailed results from the policy survey and posted comments during the open comment period, are all available on ISS' website under the Policy Gateway.

The ISS 2017 Global Policy Updates will be effective for meetings that occur on or after February 1, 2017.

The material updates to ISS' benchmark proxy voting policies are summarized below.

Americas Policy Updates

Non-Employee Director Pay – US

ISS is expanding its framework for evaluating non-employee director ("NED") pay. This policy update will provide for evaluation of a broader range of factors and more nuanced consideration of director pay with respect to (i) standalone advisory proposals seeking shareholder approval of NED pay programs and (ii) in certain cases, NED-specific equity plan proposals.

Under the expanded policy, ISS will assess director pay proposals and certain NED equity plan proposals (those determined to be relatively costly) considering 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.

Equity Plan Scorecard – US

ISS is making revisions to the factors and weightings under the U.S. Equity Plan Scorecard ("EPSC") policy. In addition to minor changes to various factor weightings, the updated policy will include one additional factor: an evaluation of the payment of dividends on unvested awards. Under this new factor, full points will be earned if the equity plan expressly prohibits for all award types the payment of dividends before the vesting of the underlying award (however, accrual of dividends payable upon vesting is acceptable). No points will be earned if this prohibition is absent or incomplete (i.e. not applicable to all award types). A company's general practice (not enumerated in the plan document) of not paying dividends until vesting will not suffice.

Modifications were also made to the minimum vesting factor. First, an equity plan must specify a minimum vesting period of one year for all award types under the plan in order to receive full points for this factor. Second, no points will be earned if the plan allows for individual award agreements that reduce or eliminate the one-year vesting requirement.

Additional information about updates to the EPSC policy will be included in ISS' Equity Compensation Plans FAQ document to be updated and published in December 2016.

Restricting Binding Shareholder Proposals – US

ISS is introducing a new policy under the Director Accountability framework to address restrictions on shareholders' fundamental right to amend the bylaws. Under the policy, ongoing adverse vote recommendations will generally be warranted for governance committee members if the company's charter imposes undue restrictions on shareholders' ability to amend the bylaws. These restrictions include but are not limited to a prohibition on the submission of binding shareholder proposals or ownership/holding requirements for such shareholder proposals that exceed those in SEC Rule 14a-8.

IPOs with Multi-Class Shareholder Structures – US

In 2016, ISS bifurcated its policy regarding action by boards to unilaterally amend bylaws and charters. The 2016 change established separate methodologies for evaluating board adoptions of bylaw or charter provisions prior to (or in connection with) a company's IPO, and unilateral adoption of bylaw and charter provisions following the completion of an IPO. In recent years, a number of companies have gone public with multi-class capital structures with unequal voting rights. Feedback from the 2016-2017 policy survey and the public comment period indicates that institutional investors view these structures as problematic. A majority of investor respondents to the policy survey favored issuing adverse vote recommendations for director nominees when a company completes its IPO with a multi-class structure, particularly where there is no pre-established sunset provision on the unequal voting rights.

For 2017, the relevant section of ISS policy will be retitled Unilateral Bylaw/Charter Amendments and Problematic Capital Structures, and adverse 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. Because a commitment to put such a provision (or a supermajority voting requirement) to a shareholder vote after the IPO is not especially meaningful when the outcome of such a vote is a foregone conclusion, the reference to a public commitment to put such provisions to a shareholder vote within three years of the IPO is being removed. However, in determining vote recommendations ISS will consider the presence of a reasonable sunset provision on the adverse governance provision(s).

Under the revised policy, at newly public companies, ISS will generally recommend withhold or against votes on 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.

Non-Employee Director Pay – Canada

ISS is introducing a case-by-case policy for TSX-listed companies to identify significant problematic non-employee director compensation practices that would result in a negative vote recommendation at the board level in addition to, or in the absence of, the ability to register a negative vote for the problematic award or payment or the plan under which it is made. For example, the issuance of excessive inducement grants to non-employee directors can create problematic incentives which may compromise an otherwise independent director's judgement or foster divergent incentives between those directors who have recently received such awards and those who have not. Similarly, the issuance of performance-based equity awards (e.g. performance share units or PSUs) to non-employee directors may increase the risk of misaligning directors' interests away from the interests of shareholders.

Under the new policy, ISS will generally recommend that shareholders withhold votes on members of the committee responsible for director compensation (or, where no such committee has been identified, the board chair or full board) where director compensation practices pose a risk of compromising a non-employee director's independence or appear problematic from the perspective of shareholders. Such practices include:

- Excessive (relative to standard market practice) inducement grants issued upon the appointment or election of a new director to the board (consideration will be given to the form in which the compensation has been issued and the board's rationale for the inducement grant);
- performance-based equity grants to non-employee directors which could pose a risk of aligning directors' interests away from those of shareholders and toward those of management; and
- other significant problematic practices relating to director compensation.

Poison Pills – Canada

ISS Canadian Voting Guidelines applicable to shareholder rights plans (poison pills) are being updated to reflect the new regulatory requirement for a minimum deposit period for all non-exempt take-over bids as set out in National Instrument 62-104 (Take-Over Bids and Issuer Bids). Whereas the current policy calls for votes against rights plans with a permitted bid minimum period greater than 60 days, the updated policy calls for votes against rights plans with permitted bid minimum periods greater than 105 days.

Board Independence – Brazil

Current ISS policy calls for boards of companies listed on the Novo Mercado and Nivel 2 segments of the Sao Paulo Stock Exchange (BM&FBovespa) to be at least 30 percent independent, but is silent on board independence at companies on the Nivel 1 and Traditional listing segments. In recognition of strong investor support for the appointment of independent directors at companies across the entire market, the new policy will call for votes against the bundled election of directors if the post-election board at a Nivel 1 or Traditional company does not have at least one independent member. While the companies listed under the Nivel 1 differentiated segment will be affected by this change in ISS policy as of Feb. 1, 2017, companies in the Traditional group will have until Feb. 1, 2018, to adjust to this new policy.

Board Independence – Argentina, Chile, Colombia, Mexico & Peru

The current policy for director elections in Latin America is based solely on the timely disclosure of the names of board nominees and does not reference a minimum independence requirement. However, the majority of the markets covered in the Latin America region already have in place some minimum independence requirements or best practice recommendations, either through hard or soft laws. Therefore, the policy is being updated to include a reference to a minimum independence market requirement or at least one independent board member, whichever is higher, to strengthen the current policy framework. Under the amended policy, a company's failure to comply with market legal requirements for minimum board independence, or its failure to appoint at least one independent board member, whichever is stricter, will be grounds for recommending votes against management nominees to the board of directors.

European, Middle East and African Policy Updates

Treatment of Employee Shareholder Representatives in Calculations of Board Independence – France

French law requires the presence of so-called Employee Shareholder Representatives (ESRs) on the board of directors of a company if employees collectively hold an interest of more than 3 percent of the share capital. Unlike employee representatives that sit on boards in France and in many other European markets, ESRs are subject to election by the general meeting of shareholders.

In principle, ESRs – as employees of the company -- can be broadly defined as non-independent directors. However, in light of the fact that the presence of ESRs on French boards of directors constitutes a legal requirement, the AFEP-MEDEF Code and the AFG (the French Association of Asset Managers) exclude ESRs when setting the minimum level of independence that boards should maintain. In other words, under the approach favored by the AFEP-MEDEF Code and AFG Guidelines, ESRs should not be counted when calculating the percentage of independent directors on a company's board.

In recognition of these market standards, ISS policy for France is being amended to exclude ESRs when calculating whether at least 50 percent of the board members elected by shareholders are independent. ESRs will thus be treated in the same way as (non-shareholder elected) employee representatives under the ISS European Voting Guidelines. This means that ESRs will not be counted when calculating the overall level of independence of board members elected by shareholders, but will be counted when calculating the overall independence of all board members.

Clarification of Overboarding Definition – Continental Europe

Under the amended policy, in **Austria**, **Belgium**, **France**, **Germany**, **Italy**, **Luxembourg**, the **Netherlands**, **Spain**, and **Switzerland**, at widely held companies, ISS will generally recommend a vote against a director candidate when s/he holds an excessive number of board appointments, as referenced by the more stringent of the provisions prescribed in local law or best practice governance codes, or as defined by the following guidelines:

- Directors who hold more than five non-chair non-executive director positions.
- A non-executive chairman who, in addition to this role, holds (i) more than three non-chair non-executive director positions, (ii) more than one other non-executive chair position and one non-chair non-executive director position, or (iii) any executive position.
- Executive directors or those in comparable roles holding (i) more than two non-chair non-executive director positions, (ii) any other executive positions, or (iii) any non-executive chair position.

An adverse vote recommendation will not be applied to a director at a company where s/he serves as CEO; instead, any adverse vote recommendations will be applied to his/her additional seats on other company boards. The same is also valid for non-executive chairmen, except (i) where they exclusively hold other non-executive chair and/or executive positions or (ii) where they are elected as non-executive chairman for the first time.

ISS will take into account board positions held in global publicly listed companies outside the same group, defined as a group of companies in which a common parent company controls at least 50 percent + 1 share of equity capital, alone or in concert.

For directors standing for (re)election at French companies, ISS will take into account board appointments as censors in French publicly listed companies.

Executive directors or those in comparable roles within investment holding companies will generally be treated similarly to non-executive directors when applying this policy.

The amendments clarify several passages in the current policy, including the definition of what constitutes an overboarded director, as well as the fact that the policy applies to executive directors or those in similar positions, meaning executives who are not necessarily members of the board, e.g. in markets with two-tiered board systems.

The amended policy also clarifies that, when calculating a director's total number of board seats, directorships in globally listed companies outside the same group are taken into account. This means that multiple directorships in listed companies within a single group (defined as a group of companies in which the parent company controls at least 50 percent + 1 share of the equity capital, alone or in concert) are considered to cumulatively constitute a single mandate, rather than multiple mandates.

The amended policy also clarifies that negative voting recommendations may be issued in cases where an overboarded director only holds non-executive chairman mandates, meaning effectively three or more non-executive chairmanships. While a safe harbor for non-executive chairmen is still considered appropriate generally, this closes a loophole in the policy that currently precludes the application of a voting sanction in these (rather anomalous) cases. The amended policy would also clarify that a negative recommendation applies when a director is being elected as chairman for the first time (i.e. when the nominee's initial election as board chairman causes him/her to exceed the allowable threshold of total board mandates defined in the policy).

Finally, the amended policy foresees exceptional treatment for executives of investment holding companies. This change recognizes that, for investment holding company executives, the participation on portfolio company boards is oftentimes integral to their role. This change is also intended to align the policy with ISS client views, as reflected in the 2015/16 policy survey.

European Pay for Performance Methodology (EP4P) – Continental Europe

After ISS introduced a pay-for-performance methodology for US companies in 2012, demand arose for a similar methodology for European companies from ISS clients and investors in general. The 2014 policy survey results revealed that 83 percent of investors who responded had indicated that a European pay for performance quantitative methodology, including the use of peer group comparisons, would be useful as a factor in such evaluations. ISS developed a European Pay for Performance (EP4P) methodology for European companies in 2015 and introduced it in 2016.

ISS' European Guidelines refer to principles of good stewardship with respect to remuneration practices and seek a reasonable alignment between pay and performance. In 2016, ISS referred to the quantitative pay-for-performance assessment in its reports on continental European companies. However, the current European Voting Guidelines do not explicitly refer to the EP4P methodology. During the 2016 proxy season, this methodology was successfully implemented and feedback from the 2016 ISS policy survey indicates that a majority (92 percent) of investor respondents support the use of the EP4P model outcome as a contributing factor within the current holistic approach. Therefore, an explicit reference to the EP4P methodology is being added to the European Voting Guidelines to further clarify the guidelines and ensure global consistency.

Also, Principle 2 under the executive remuneration section in European voting guideline requires clarification in order to better reflect Principles 2.1 to 2.3, which are focused on the pay structure and the emphasis on long-term shareholder value. The wording of Principle 2 is being amended to state that companies should maintain an appropriate pay structure with emphasis on long-term shareholder value creation.

Non-Executive Director Remuneration – Continental Europe

Grants of performance-based cash and performance-based equity compensation to non-executive directors are relatively rare among publicly listed companies in most continental European markets, as these practices are widely viewed by investors as being potentially compromising of director independence. Notably, the International Corporate Governance Network and a number of prominent European codes of best practice recommend against these practices. Also, many ISS clients based in continental Europe have customized voting policies that oppose the grant of performance-based compensation of all forms to non-executive directors. ISS policy is being amended to clarify that ISS will recommend a vote against any proposals providing for the granting of stock options, performance-based equity compensation (including stock appreciation rights and performance-vesting restricted stock), and performance-based cash to non-executive directors.

Clarification of Overboarding Definition – UK/Ireland

The UK/Ireland policy is being amended to clarify potentially ambiguous language as to the acceptable number of directorships, and to clarify that an individual who holds multiple chair roles but no non-chair director roles could receive an adverse vote recommendation for overboarding. Under the revised policy, where directors have multiple board appointments, ISS may recommend a vote against directors who appear to hold an excessive number of board roles at publicly-listed companies, defined as follows:

- Directors who hold more than five non-chair non-executive director positions.
- A non-executive chairman who, in addition to this role, holds (i) more than three non-chair non-executive director positions, (ii) more than one other non-executive chair position and one non-chair non-executive director position, or (iii) any executive position.
- Executive directors holding (i) more than two non-chair non-executive director positions, (ii) any other executive positions, or (iii) any non-executive chair position.

When applying this policy, ISS will consider the nature and scope of the various appointments and the companies concerned, and if any exceptional circumstances exist. A stricter view may apply for directors who serve on the boards of complex companies, those in highly regulated sectors, or directors who chair a number of key committees.

An adverse vote recommendation will not be applied to a director within a company where he/she serves as CEO; instead, any adverse vote recommendations will be applied to his/her additional seats on other company boards. The same is also valid for chairmen, except (i) where they exclusively hold other chair and/or executive positions or (ii) where they are elected as chairman for the first time.

Remuneration – UK/Ireland

The wording of the remuneration sections will be amended to reflect developments in UK market practice and investor expectations surrounding remuneration.

- Introduce a direct reference (in the introduction section) to companies that seek to implement pay structures (for example non-performance related restricted shares) which sit outside of the typical UK model, to make it clear that a greater level of certainty of reward should be matched by lower award levels;
- Introduce a reference to a potential recommendation against the chair of the remuneration committee when serious issues are identified;
- For the remuneration report resolution, introduce a reference to the use of ISS' Pay-for-Performance methodology (EP4P) and also include a definition of EP4P; and
- For the remuneration report resolution, clarify that in termination scenarios, appropriate pro-rating on outstanding share awards should be applied.

The changes to the policy reflect some of the main issues which are expected to be relevant for 2017, when many UK companies will be seeking shareholder approval for new (binding) remuneration policies. The new paragraph added to the introductory section of the policy document directly addresses the recommendation of the Investment Association's Executive Remuneration Working Group for companies to consider pay models which do not fully align with the typical structure found in the UK market. This is accompanied by related changes to the wording of the specific sections of the voting guidelines on remuneration policy and remuneration report resolutions.

The extension of the policy to potentially recommend against the chair of the remuneration committee in the event of a serious breach of good practice reflects the position of some investors that the committee chair should be held directly accountable where major remuneration issues have been identified. This approach of escalation is also consistent with the voting guidelines of the Pensions and Lifetime Savings Association (PLSA), which have historically formed the basis for much of the content of ISS' UK & Ireland voting guidelines.

The current UK & Ireland guidelines do not explicitly refer to ISS' EP4P methodology. As noted above, ISS developed this methodology for European companies in 2015 and introduced it in 2016. The implementation of the methodology was successful and investors support the use of the EP4P model outcome as a contributing factor within the overall approach to examining remuneration. Therefore, a reference to the model will be introduced to the UK & Ireland guidelines as a factor to take into account in considering remuneration report resolutions.

Board and Committee Composition – UK Smaller Companies

ISS policy is being amended to clarify that the policy for AIM companies also applies to certain other companies, and to bring the policy into line with the Quoted Companies Alliance (QCA) Code by specifying that audit and remuneration committees should be fully independent. ISS will apply this standard with effect from February 2018, in recognition of the significant nature of the change and to give small companies time to comply with this standard if they wish to do so.

The new policy states that ISS will generally recommend votes for the election or re-election of directors, unless:

- Adequate disclosure has not been provided in a timely manner;

- The board fails to meet minimum corporate governance standards – please see the following sections on independence classification and board and committee composition for details of how this is interpreted in practice; or
- There are specific concerns about the individual, such as his/her ability to commit sufficient time to the role.

The requirements for FTSE Fledgling companies are the same as for FTSE SmallCap companies, as set out in the core policy. This means that the **board** should include a minimum of two independent non-executive directors. The **audit** and **remuneration** committees should be fully independent, and should include a minimum of two independent non-executives. For the board and the audit and remuneration committees, the board chairman cannot count as one of the independent directors. The majority of the members of the **nomination** committee should be independent.

The chairman may sit on all committees provided that he/she continues to be considered independent.

For companies listed on AIM, and for other companies which are not a member of the FTSE All Share or FTSE Fledgling Indices and in line with the QCA Code, the audit and remuneration committees should include independent non-executive directors only, and half the members of the nomination committee need to be independent.

For all companies, executive directors should not serve on the audit or remuneration committees.

Asia-Pacific Policy Updates

Creation of Advisory Positions (Sodanyaku or Komon) – Japan

Many Japanese companies employ former senior executives in an advisory capacity, often for many years after they retire from their executive posts. These advisors typically receive compensation and benefits from the company, and continue to maintain an office there; however, unless the advisors remain on the board of directors, there is rarely any disclosure of their activities or their compensation, and they owe no fiduciary duties to shareholders. The influence and lack of accountability of corporate advisors have attracted considerable negative attention in recent years, in particular in connection with the accounting scandal at Toshiba Corp., which employed three former presidents in advisory capacities. Commentators have noted that the presence of former senior executives makes it difficult for their successors to reverse course on their predecessors' strategic decisions, even when doing so would be good for the company. Furthermore, the continued employment of former executives by their "home companies" reduces the pool of available candidates to serve as outside directors at other firms, contributing to Japan's low level of board independence.

Accordingly, under the new policy ISS will generally recommend votes against amendments to articles of incorporation to create new advisory positions such as "sodanyaku" or "komon," unless the advisors will serve on the board of directors and thus be fully accountable to shareholders. About 30 percent of Japanese companies' articles authorize the appointment of advisors. Most of these provisions have been in place for many years, however, and in any given year relatively few companies seek shareholder approval to add such authorization to their articles. However, while few companies will be directly impacted by the new ISS policy, the policy is intended to signal to the broader market that investors are concerned about the corporate advisors' lack of accountability and would like to see companies abandon an outdated practice that provides little or no benefit to shareholders.

Board Independence and Lead Independent Directors – Singapore

The Singapore Code of Corporate Governance now calls for issuers to appoint a lead/senior independent director when (i) the chairman and CEO posts are held by the same person, (ii) the chairman is an immediate family member of the

CEO, (iii) the chairman is part of the management team, or (iv) the chairman is otherwise not independent. The Singapore Code also calls for boards to be at least 50 percent independent in these circumstances. Following a transition period, these provisions will be fully applicable to annual meetings held on or after Oct. 1, 2017. In line with these revisions to the Singapore Code, ISS will generally recommend votes against members of a company's nomination committee if the company has not appointed a lead/senior independent director or has a board independence level of less than 50 percent in situations where the board chairman is not independent.

Overboarding – India

The Indian Listing Agreement was recently amended to provide that a person shall not serve as an independent director of more than seven listed companies, and a person who is serving as an executive director of any listed company shall serve as an independent director of not more than three listed companies. In view of the changes in the regulations, it was deemed timely to introduce an overboarding policy for India. The new policy defines "overboarding" as directorships at more than six listed companies, which is in line with ISS overboarding policies applied to regional peers such as Hong Kong and Singapore.

Election of Directors & Supervisors – Taiwan

The election of directors and supervisors in Taiwan is unique. Legal entities such as governmental organizations and corporations, not just natural persons, can serve as non-independent directors and supervisors. Legal entities can either appoint individuals as candidates or run for election themselves and then appoint representatives to perform the fiduciary duties. As a result, it is not uncommon in Taiwan to see only the name of the legal entity being nominated for a board seat and not the identity of the actual individual who will serve on the board to represent that entity's interest.

Another notable characteristic in Taiwan is that only the independent directors are elected by the standard nomination system. The election of non-independent directors and supervisors, on the other hand, may use a traditional election system which is commonly referred to as the "non-nomination" system. Under this non-nomination system, any shareholder can nominate any person of legal age to the board. Companies are not obliged to provide a roster of candidates and their profiles before the meeting, and many firms disclose candidate names and profiles at the meeting or only a few days beforehand. Further, whether or not the candidates are supported by management is often not disclosed.

Election by the non-nomination system poses a great challenge to investors, particularly overseas investors voting by proxy who must cast their votes well in advance of the meeting. The non-nomination system disenfranchises minority shareholders and greatly limits their ability to cast informed votes. The lack of timely disclosure also makes it impossible to apply voting policies based on attendance, overboarding, or other commonly-used criteria. In contrast, under the nomination system, the board of directors reviews the qualifications of each candidate nominated by either the board itself or any shareholder holding one percent or more of the company's outstanding shares, and then provides the final roster of candidates together with their profiles to shareholders prior to the meeting.

The amended Taiwan policy will continue to recommend votes against all directors and supervisors where the company employs the non-nomination system. When the company employs the nomination system, the amended policy provides that ISS will generally recommend votes for all non-independent director and supervisor candidates. ISS will generally recommend votes for independent director nominees, unless:

- The nominee is a legal entity or a representative of a legal entity;
- The nominee has attended less than 75 percent of board and key committee meetings over the most recent fiscal year, without a satisfactory explanation. The calculation of director attendance (or that of the representatives appointed by a legal entity which serves as a corporate director in the company) will not include meetings attended by alternate directors (or the proxy of those representatives). Acceptable reasons for director absences are generally limited to the following:

  - Medical issues/illness;
  - Family emergencies;
  - The director (or the representative) has served on the board for less than a year; and
  - Missing only one meeting (when the total of all meetings is three or fewer);
- The nominee sits on more than six public company boards; or
- The nominee has been a partner of the company's auditor within the last three years, and serves on the audit committee.

Furthermore, the new policy calls for votes against directors or supervisors, members of a committee, or the entire board, due to:

- Material failures of governance, stewardship, risk oversight, or fiduciary responsibilities at the company;
- Failure to replace management as appropriate; or
- Egregious actions related to a director's or supervisor's service on other boards that raise substantial doubt about his or her ability to effectively oversee management and serve the best interests of shareholders at any company.

In making any of the above recommendations on the election of directors, ISS generally will not recommend against the election of a CEO, managing director, executive chairman, or founder whose removal from the board would be expected to have a material negative impact on shareholder value.

Furthermore, the new policy provides a framework for voting on director nominees in contested elections in Taiwan, including the election of shareholder nominees or the dismissal of incumbent directors.

For shareholder nominees, ISS places the burden of proof on the nominee or the proposing shareholder to persuade shareholders that they are better suited to serve on the board than management's nominees. Serious consideration of shareholder nominees will be given only if there are clear and compelling reasons for the nominee(s) to join the board. These nominees must also demonstrate a clear ability to contribute positively to board deliberations; as some nominees may have hidden or narrow agendas and may unnecessarily contribute to divisiveness among directors.

The major decision factors are:

- Company performance relative to its peers,
- Strategy of the incumbents versus the dissidents,
- Independence of directors/nominees,
- Experience and skills of board candidates,
- Governance profile of the company,
- Evidence of management entrenchment,
- Responsiveness to shareholders, and
- Whether a takeover offer has been rebuffed.

APPENDIX

Summary of Comments from 2016 Comment Period for 2017 Policies

The majority of public comments this year related to the proposed policy change related to general share issuance authorities (share issuance mandates) at US-listed cross-market companies that are required by the laws of their country of incorporation to seek shareholder approval of any share issuances. Additional comments related to evaluation of compensation-related votes at cross-market companies, companies that go public with multi-class share structures, shareholders' inability to amend company bylaws, the European pay for performance model, non-executive director remuneration and director overboarding.

The proposed policy on share issuance mandates was intended to fill a gap in ISS's US benchmark policy to address the increasing number of formerly US-domiciled companies which have reincorporated overseas and are now required to obtain shareholder approval to issue new shares. To avoid the need to seek separate approval for every issuance, companies domiciled in markets such as the UK, Ireland, the Netherlands and Singapore generally seek approval at their annual meeting for a general authority, or mandate, covering share issuances during the coming year (or in some cases a longer period), up to a specified limit. In the absence of a US policy covering such general share issuance authorities, ISS has been applying the policy of the market of incorporation, as that is the market which caused the proposal to appear on the ballot. Those policies are generally based on local listing rules and codes of best practice, which are often considerably more stringent than local corporate laws. However, the best practice provisions are intended to apply to companies with a listing in that market, and those policies generally do not reflect the rules applicable to companies with a US listing.

The aim of the proposed policy was to reflect US rules and investor expectations, while still providing safeguards against excessive dilution to shareholders' ownership interests. Many investors view 20 percent to be a significant level of dilution, and NYSE and NASDAQ listing rules require a shareholder vote on issuances above 20 percent in certain circumstances. The policy proposal would have supported a mandate for share issuances up to 20 percent, meaning that companies would have to seek specific approval for larger issuances – thereby in effect extending the NYSE and NASDAQ approval requirements to situations where a shareholder vote is not currently required, such as private placements not at a discount or public offerings for cash. (As preemptive rights have effectively disappeared from US capital markets, the 20 percent limit would apply to share issuances without preemptive rights, which are subject to more restrictive limits in markets such as the UK and Ireland than preemptive issuances.)

Comments on the proposed policy came predominantly from corporate issuers (primarily those incorporated in Ireland) and law firms representing such companies. Commenters expressed concern that such a rule would put cross-market companies at a disadvantage in share-based acquisitions relative to US-domiciled rivals who would be able to offer greater speed and certainty of being able to issue the necessary shares. (This would apply, for example, in cases where a company makes multiple small-scale share-based acquisitions during a year that individually would not trigger US listing requirements for a shareholder vote but that collectively exceed 20 percent of issued capital.) Commenters further questioned whether these companies' primarily US-based shareholders are really concerned with dilution, or are interested in safeguards beyond those currently provided by US listing rules.

Several companies listed in the US but incorporated in the UK or Switzerland commented on ISS' analytical approach when multiple compensation-related proposals appear on ballots due to SEC rules and company laws in the market of incorporation. These companies favored alignment of ISS voting recommendations to avoid inconsistent recommendations with respect to a single pay program, and emphasized that as US-listed companies with a majority-US investor base, their compensation practices for both officers and directors are primarily driven by US practices and the concerns expressed by US investors.

The Council of Institutional Investors weighed in regarding companies that go public with a multi-class capital structure. The CII noted its members' belief that "the most appropriate approach to equity structure for IPO companies is 'one share, one vote'," and stated that for the minority of companies that choose to go public with a multi-class share structure with unequal voting rights, "it is critical that the governing documents include meaningful sunset provisions." The CII commented further that an appropriate sunset provision could be based on time elapsed since the IPO, on levels of ownership by insiders, or a hybrid of these two approaches, and stated that the precise terms of an appropriate sunset provision would depend on company- and industry-specific factors such as up-front investment needs, the length of the business cycle and a company's susceptibility to "premature acquisition." Finally, the CII offered examples of sunset provisions its staff viewed as "clearly unreasonable," such as one company's provision that the multi-class structure would be phased out after 17 years, and another company's pledge to collapse the multi-class structure if the superior class constitutes less than 5 percent of voting power.

On the same topic, an institutional investor based in Europe offered the opinion that sunset provisions for multi-class share structures or other adverse governance structures should be strictly time-based, with a duration of no more than five years, while a US company commented that "issuers should have the discretion to determine the sunset provisions and underlying criteria for multi-class capital structures on a case-by-case basis." Finally, the US Chamber of Commerce Center for Capital Markets Competitiveness suggested that companies unable to insulate their management teams from the "sudden pressure to satisfy short-term performance objectives once the company goes public" might choose not to go public at all, and suggested that investors who disagree with a company's choice of capital structure invest elsewhere.

On the matter of non-executive director pay in Canada, a Canadian institutional investor and one based in Europe both expressed opposition to the payment of "inducement grants" to non-executives joining the board, and to the grant of any performance-based equity awards to non-executive directors. The two investors likewise opposed the grant of performance-based pay (equity or cash) to non-executive directors in Europe, and neither investor supported making an exception for Germany, where performance-based pay has been viewed as acceptable. However, one German company wrote in to defend the use of performance-based compensation for non-executive directors, as long as it is "designed to incentivize the orientation of the company to sustainable long-term growth" and not based on short-term performance.

Finally, the European pay-for-performance (EP4P) methodology drew a number of comments from investors and corporations. The aforementioned European and Canadian institutional investors agreed that pay quantum or magnitude is important; that misalignment between pay and performance may signal additional governance risks, and that remuneration-related concerns could be grounds for voting against members of the remuneration committee. Comments submitted by a consulting firm, on behalf of a group of Swiss companies, noted that under Swiss law investors are already considering pay quantum under the binding AGM remuneration votes, but expressed caution about the use of a P4P "formula" in determining votes on these binding resolutions. The Swiss companies were concerned about an overemphasis on relative TSR as the measure of performance, and favored giving discretion to remuneration committees to define performance more broadly and to select appropriate comparator companies. The comment letter further stated that a P4P misalignment "will generally not be indicative of potential governance risks."

The comment period is an important part of our policy development process, providing an opportunity for ISS to review and consider feedback on key policy changes from institutional investors, corporate issuers, and other market constituents. With respect to the proposed creation of a US policy on share issuance mandates, ISS has decided to continue to study this issue and to seek additional client input to determine whether the proposed policy is the best way to achieve the stated goals. This deliberation will be informed by factors including NASDAQ's recent solicitation of public comment on changes to Listing Rule 5635, which could result in narrowing the circumstances in which a shareholder vote on new share issuances is required; and potential changes to US tax laws which could reverse the trend toward redomestication out of the United States. Accordingly, ISS will not introduce a new policy on general share issuance authorities for US-listed companies at this time.

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