Independent Chair Shareholder Proposals (U.S.)

Background and Overview

Calls for independent board chairs were the most prevalent type of shareholder proposal offered for consideration at U.S. companies' annual meetings in 2014. As of June 30, 62 of these proposals have come to a shareholder vote, up from 55 resolutions over the same time period in 2013. Notably, the number of proposals calling for independent board chairs has more than doubled over the past five years. Under the current policy formulation, ISS recommended against 32 of these 62 proposals in 2014. In line with results from recent seasons, independent chair proposals received average support of 31.2 percent of votes cast at 2014 meetings. Only four of these proposals received the support of a majority of votes cast.

Recent high-profile board leadership changeovers at Hewlett-Packard and Bank of America may focus investors' attention on directors' decisions to revert to a combined CEO/chair role after years of independent leadership. Notably, at Bank of America, a shareholder-sponsored bylaw amendment mandating an independent chair received majority support from shareholders in 2009. The company's board repealed this provision to allow it to recombine the titles (and created a new lead director position).

Regarding the presence of an executive or non-independent chair in addition to the CEO, a recent academic study[1] found that retention of a former CEO in the role of chair may prevent new CEOs from making performance gains by dampening their ability to make strategic changes at the company. In addition, it is debatable whether a lead independent director can act as an effective counterbalance to both a CEO and an executive chair.

ISS' current policy is to generally recommend for independent chair shareholder proposals unless the company satisfies all of the following criteria:

- The company designates a lead director, who is elected by and from the independent board members with clearly delineated and comprehensive duties.
- The board is at least two-thirds independent.
- The key board committees are fully independent.
- The company has disclosed governance guidelines.
- The company has not exhibited sustained poor TSR performance (defined as one- and three-year TSR in the bottom half of the company's four digit industry group, unless there has been a change in the CEO position within that time).
- The company does not have any problematic governance issues.

[1] Quigley, Timothy J. and Hambrick, Donald C., When the Former CEO Stays on as Board Chair: Effects on Successor Discretion, Strategic Change, and Performance (December 6, 2010). Strategic Management Journal, 33: 834–859, DOI: 10.1002/smj.1945, July 2012.

Key Changes under Consideration

ISS proposes to update the “Generally For” policy by adding new governance, board leadership, and performance factors to the analytical framework and to look at all of the factors in a holistic manner. Notably, the policy update would add new factors that are not considered under the current policy including the absence/presence of an executive chair, recent board and executive leadership transitions at the company, director/CEO tenure, and a longer (five-year) TSR performance period.

Intent and Impact

ISS believes that a more holistic review of each company's board leadership structure, governance practices, and financial performance will strengthen the application of this policy. Under the proposed revisions, any single factor that may have previously resulted in a "For" or "Against" recommendation may be mitigated by other positive or negative aspects, respectively.

While the impact of this proposed policy on independent chair shareholder proposals in 2015 cannot be determined at this time, backtesting of the new methodology using data for the companies targeted in 2014 resulted in a higher level of support for the resolutions.

Request for Comment

While we appreciate any comments on this topic, ISS seeks specific feedback on the following issues.

1. What factors does your organization consider most important when determining whether an independent chair shareholder proposal warrants support?

2. How much weight does your organization give to recent changes in board leadership structure (e.g., a switch from an independent chair to a non-independent chair; a recombination of the CEO/chair roles)? Please specify issues and relative weights.

3. What timeframe should ISS use when assessing financial performance when evaluating independent chair proposals?

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