



CORPORATE GOVERNANCE UPDATE

ISS Publishes Policy Updates for 2012 Proxy Season

On November 17, 2011, Institutional Shareholder Services Inc. (“ISS”) published corporate governance policy updates (the “Policy Updates”) to its benchmark proxy voting guidelines. The Policy Updates will apply to shareholder meetings held on or after February 1, 2012. The complete text of the *U.S. Corporate Governance Policy – 2012 Updates* can be found [here](#).¹ We summarize below what we believe to be the most significant of the Policy Updates.

TOPIC	SUMMARY OF POLICY UPDATE
<i>Pay-for-Performance Evaluation</i>	<p>ISS’s pay-for-performance assessment has been and continues to be crucial in determining what vote ISS will recommend with respect to compensation committee members and say-on-pay proposals. Perhaps the most significant of the Policy Updates is that ISS has changed the method by which it will assess pay-for-performance. Under the old method, ISS looked at an issuer’s total shareholder return (TSR) performance against a peer group comprised of other issuers with the same GICS code. If that performance was in the bottom half of its peer group for the most recent one-year and three-year periods, ISS assessed whether CEO pay was in line with such performance.</p> <p>For 2012, ISS will employ a new methodology. In 2012, for companies in the Russell 3000 Index, ISS will begin its pay-for-performance evaluation with two quantitative tests referred to as “peer group² alignment” and “absolute alignment.” For the peer group alignment test, ISS will review (i) the “degree of alignment” between the company’s TSR rank and CEO pay rank within a peer group, as measured over one-year (weighted 40%) and three-year (weighted 60%) periods, and (ii) the multiple of the CEO’s total pay relative to the peer group median. For the absolute alignment test, ISS will look at the difference between the trend in annual changes in CEO pay and the “trend” in annualized TSR over the prior five fiscal years.</p> <p>If the initial quantitative tests demonstrate significant weak pay-for-performance alignment, ISS will conduct a qualitative analysis to determine whether there are causal or mitigating</p>

¹ An ISS-prepared summary of the Policy Updates is available [here](#).

² ISS will construct peer groups of 14-24 companies in a comparable industry and size range based on market cap and revenue (or assets for financial firms), utilizing the Global Industry Classification Standard (GICS). ISS plans to publish its peer group methodology and rationale in advance of the 2012 proxy season to provide more details as to how ISS forms its peer groups.

factors at play, looking at items such as (i) the ratio of performance- to time-based equity awards, (ii) the ratio of performance-based compensation to overall compensation, (iii) the completeness of disclosure and rigor of performance goals, (iv) the company's peer group benchmarking practices, (v) actual results of financial/operational metrics (e.g., growth in revenue, profit, cash flow) both in absolute terms and relative to peers, (vi) special circumstances (e.g., a new CEO in the prior fiscal year or anomalous grant practices) and (vii) any other factors ISS deems relevant.

Unfortunately, there is a tremendous amount that is unclear regarding the new methodology. ISS has not yet said, for example, what level of misalignment it will consider problematic enough to trigger its review of the qualitative factors identified above. ISS has indicated that it plans to release additional guidance in December 2011.

*Board Response to
Significant Dissent on
Say-on-Pay Vote*

One of the big uncertainties heading into the 2012 proxy season was the level of shareholder opposition to 2011 say-on-pay resolutions that ISS would consider problematic. In the Policy Updates, ISS clarified that if a company's 2011 say-on-pay proposal received the support of less than 70% of the votes cast by shareholders, ISS will apply heightened scrutiny and develop its voting recommendations on a case-by-case basis with respect to the re-election of compensation committee members and the company's 2012 say-on-pay proposal.

In its case-by-case analysis, ISS will take into account (i) the company's response to the low level of shareholder support, including (x) disclosure of engagement efforts with major institutional investors regarding the compensation issues that led to the significant dissent, (y) specific actions taken to address such compensation issues and (z) other recent compensation actions taken by the company, (ii) whether the compensation issues raised are one-time versus recurring, (iii) the company's ownership structure and (iv) whether the level of shareholder support was less than 50%, in which case ISS will expect the highest degree of responsiveness.

*Board Response to
Frequency Vote
Results*

As expected, ISS announced that it will not react favorably in those presumably infrequent instances in which a company elects a frequency for its say-on-pay votes that is inconsistent with the frequency favored by shareholders at the 2011 Annual Meeting. Specifically, ISS has indicated that it will recommend a vote against all incumbent directors if the company will hold future say-on-pay votes less frequently than the frequency that received a majority of the votes cast by shareholders at the 2011 annual meeting. If no frequency was preferred by a majority of the votes cast, ISS will recommend voting on a case-by-case basis on the entire board if the company will hold future say-on-pay votes less frequently than the frequency that received a plurality of the votes cast by shareholders.

*Proxy Access
Proposals*

Given the effectiveness of the proxy access-related amendments to Rule 14a-8, there was considerable curiosity regarding the policy that ISS would adopt regarding proxy access proposals. Unfortunately, ISS has not provided clear guidance on this topic. Rather, it has said in the Policy Updates that it will evaluate proxy access proposals on a case-by-case basis. The company-specific and proposal-specific factors it will consider in its evaluation include (i) the percentage and duration of ownership proposed in the proposal, (ii) the maximum proportion of directors that shareholders may nominate each year, (iii) the method of determining which nominations should appear on the ballot if multiple shareholders submit nominations and (iv) any other factors ISS deems relevant, including the proponent's rationale for the proposal.

ISS intends to apply these same factors to proxy access proposals submitted by management as well as shareholders. ISS has indicated that it will release additional guidance in January 2012 upon its review of proxy access proposals that are actually submitted.

*Exclusive Venue
Proposals*

The 2011 proxy season saw the emergence of management proposals seeking shareholder approval of charter provisions selecting Delaware as the exclusive venue for certain types of litigation brought against the issuer and its directors and officers. ISS's current policy is to vote against exclusive venue proposals unless the company has adopted specified best-practices governance features. In the Policy Updates, ISS indicated that it will evaluate exclusive venue proposals on a case-by-case basis in 2012, taking into account the company's litigation history and whether the following governance features are in place at the company: majority voting, annually-elected directors and the absence of a poison pill (unless it was approved by shareholders).

*Political Spending
Proposals*

According to ISS, approximately 1/3 of the shareholder resolutions on environmental and social issues voted on in 2011 dealt with political contributions as shareholders seek greater disclosure of corporate practices regarding political spending and activities. ISS currently reviews proposals requesting enhanced disclosure of a company's political contributions and trade association spending on a case-by-case basis. In 2012, ISS will generally recommend a vote in favor of political spending proposals, but only after explicitly considering (i) the company's existing disclosure of policies and oversight mechanisms related to political contributions and payments to trade associations and (ii) recent significant controversies, fines or litigation related to the company's political contributions or activities.

If you have any questions regarding this update, please contact the Sidley lawyer with whom you usually work.

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