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ISS and Glass Lewis Publish 2017 U.S. Voting Policies

U.S. proxy advisory firms Institutional Shareholder Services and Glass Lewis have issued their respective voting policies for the 2017 proxy season. Both sets of updates are relatively light compared to some prior years and show a consensus in approach between the two firms on certain issues, including increased scrutiny of governance structures at newly public companies and a continued focus on board composition. We summarize key updates below.

ISS U.S. Policy Updates

Shareholder Rights – Ability to Amend Bylaws

ISS adds a new policy to issue adverse vote recommendations for governance committee members if the company's charter imposes undue restrictions on shareholders' "fundamental right" to amend the bylaws. Such restrictions include a prohibition on the submission of binding shareholder proposals or the imposition of ownership or holding period requirements for shareholder proposals that are more onerous than the de minimis thresholds set by Exchange Act Rule 14a-8 (i.e., at least $2,000 in market value, or 1%, of the company's securities entitled to be voted on the proposal at the meeting, and held for at least one year by the date of the submission of a proposal and through the meeting date).

Newly Public Companies with Multi-class, Unequal Voting Structures

In 2016, ISS instituted a policy whereby it would generally recommend against individual directors or the whole board (except new nominees which ISS considers on a case-by-case basis) if the board adopts bylaw or charter provisions that are materially adverse to shareholder rights even in the IPO context. In making its decision, ISS would consider factors including the level of impairment of shareholder rights caused by the provision, the disclosed rationale for the provision, the impact on shareholders' ability to change the governance structure in the future (e.g., limitations on shareholders' rights, or supermajority vote requirements, to amend the bylaws or charter), whether there is a classified board and whether there is a public commitment to put the provision to a shareholder vote within three years of the IPO. ISS would continue this review until the adverse provision is reversed or submitted for shareholder approval.

Starting with the 2017 proxy season, ISS will apply the same policy and methodology to newly public companies with multi-class capital structures where the classes do not have identical voting rights. In addition, for both shareholder-adverse bylaw and charter provisions and multi-class capital structures, a commitment to put the particular provision or structure to shareholder approval will no longer be

sufficient to affect ISS' adverse vote recommendation; instead, a reasonable sunset provision would be needed.

Overboarded Directors

As previewed last year, starting in 2017, directors who sit on more than five public company boards (previously six) will receive adverse vote recommendations. No changes were made to ISS' CEO director overboarding policies, which still state that CEOs of public companies who sit on the boards of more than two public companies besides their own will receive adverse recommendations at their outside boards.

Director Compensation

ISS has adopted a new policy for 2017 with respect to management proposals seeking ratification of non-employee director compensation. ISS will review the proposals on a case-by-case basis and will evaluate such arrangements based on eight qualitative factors, including, the (i) amount of director compensation as compared to similar companies, (ii) any problematic pay practices relating to director compensation, (iii) director stock ownership guidelines and holding requirements, (iv) equity award vesting schedules, (v) mix of cash and equity-based compensation, (vi) meaningful limits on director compensation, (vii) availability of retirement benefits or perquisites and (viii) quality of the disclosure of director compensation. In addition, if the equity plan under which non-employee director grants are made is on the ballot, ISS will consider whether it warrants support.

Evaluation of Equity and Cash Plans

ISS uses an equity plan scorecard for equity-based plans. ISS added an additional factor to its equity plan scorecard, which evaluates whether approving an equity plan is in the shareholders' best interest, and made minor changes to its factor weightings under the scorecard. ISS will now consider whether a plan provides for payment of dividends to holders of unvested awards, and full points will be earned on the scorecard only if the plan expressly prohibits payment of dividends on all types of unvested awards (although dividends on unvested awards may be accrued). No points will be earned if the prohibition on paying dividends is absent or not in all awards. In addition, with respect to the minimum vesting factor, the plan must specify a minimum vesting period of one year to receive full points and no points will be earned for such factor if the plan permits individual award agreements to reduce or eliminate the one-year vesting requirement. ISS will provide additional information about updates to its equity plan scorecard policy in December 2016 when it issues updated FAQs.

ISS revised its voting policy for amendments to cash and equity compensation plans to differentiate the framework applicable to amendment proposals presented only for Section 162(m) purposes (provided such plan is administered entirely by independent outsiders based on ISS' categorization of independence) from those proposals presented for multiple purposes beyond Section 162(m) (such as

increased shares or amendments which may result in increased cost). ISS has clarified that it will vote against a proposal presented only for Internal Revenue Code Section 162(m) purposes if the compensation committee is not independent.

With respect to non-employee director equity plans (which are not subject to ISS' equity plan scorecard), ISS revised its voting policy to provide that such plans be evaluated on a case by case basis based on the same qualitative factors used for evaluating non-employee director compensation arrangements (as described above), which includes additional factors (including relative pay magnitude and meaningful pay limits) and broadens and clarifies existing factors currently used by ISS. ISS has clarified that when a non-employee director plan is determined to be relatively costly, ISS will review it on a case-by-case basis, looking holistically at all the factors rather than requiring that all enumerated factors meet certain criteria.

Other Amendments

ISS also clarified that it will recommend management proposals to increase common stock authorizations for stock splits and stock dividends by examining the effective increase pursuant to its general common stock authorization policy.

For ISS' policy updates, see http://www.issgovernance.com/policy-gateway/2017-policy-information/. As a reminder, ISS often publishes additional policy FAQs as the proxy season progresses, so additional changes and guidance may still be forthcoming.

Glass Lewis U.S. Policy Updates

Shareholder Rights – Enhanced Scrutiny of IPO/Spin-Off Company Governance

Glass Lewis has generally given newly public companies a one-year grace period with respect to governance practices. Starting in 2017, Glass Lewis will review a newly public company's governance from the outset to determine whether shareholder rights are being "severely restricted indefinitely." This includes considerations of whether the company has adopted certain antitakeover protections (in particular a pill or classified board), supermajority vote requirements to amend governing documents, fee-shifting bylaws or exclusive forum provisions; whether shareholders have the ability to call special meetings, act by written consent and remove directors without cause; which director election standards apply and whether there are evergreen provisions in company equity compensation arrangements. If these anti-takeover provisions are present, Glass Lewis will consider recommending against directors if there is no commitment to submit the provision to a shareholder vote at the next annual meeting after the company goes public or a sound rationale or sunset provision for the takeover provision.

Overboarded Directors

Also previewed last year, Glass Lewis has changed its overboarding policies such that it will now generally recommend against a director who serves as an executive officer of any public company while serving on a total of more than two public company boards (previously three) and any other director who serves on a total of more than five public company boards (previously six). Exceptions may be available if a company provides sufficient rationale for the directors continued service.

Board Refreshment/Evaluations

Glass Lewis has clarified that it is focusing more on whether companies have a robust board evaluation process (i.e., one focused on the assessment and alignment of director skills with company strategy) because it believes that such procedures would be more effective than reliance on age or tenure limits.

For the Glass Lewis policy updates, see http://www.glasslewis.com/resource/guidelines/.

Glass Lewis also published a 2017 update to its Shareholder Initiatives policy, with the only highlighted change being the codification of its policy on shareholder proposals requesting companies to provide increased disclosure on gender pay equity. For the Shareholder Initiatives update, see http://www.glasslewis.com/wp-content/uploads/2016/11/2017_GUIDELINES_Shareholder_Initiatives.pdf.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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