

Memorandum

ISS Issues Draft Voting Policy Changes, Requesting Comment

November 2, 2016

On October 27, 2016, Institutional Shareholder Services Inc. (“ISS”) issued proposed changes to its proxy voting policies, seeking comment from all interested market constituents.¹ ISS will accept comments through November 10, 2016 at 6 p.m. Eastern Time. If adopted, ISS’s proposed policy changes will take effect for meetings occurring on or after February 1, 2017. ISS plans to release its final 2017 policies during the week of November 14, 2016.

ISS proposes four changes that will affect issuers subject to its U.S. proxy voting guidelines; two of these proposed changes would affect only U.S.-listed companies incorporated outside the U.S.

1. Unilateral Board Actions

Under ISS’s current policy, adopted in 2014, ISS generally recommends a vote against or withhold from individual directors, committee members, or the entire board if the board unilaterally amends the company’s bylaws or charter “in a manner that materially diminishes shareholders’ rights or that could adversely impact shareholders,” taking several factors into account. ISS updated this policy last year to add that, in subsequent years, it will recommend a vote case-by-case on director nominees “[u]nless the adverse amendment is reversed or submitted to a binding shareholder vote.” However, when a board unilaterally amends the company’s governing documents to classify the board, establish supermajority voting requirements to amend the bylaws or charter, or eliminate shareholders’ ability to amend the bylaws, ISS will generally recommend a vote **against** director nominees in subsequent years until the unilateral action is either reversed or submitted to a binding shareholder vote.

In addition, as amended last year, ISS’s policy provides that if a board amends the company’s bylaws or charter prior to or in connection with the company’s initial public offering (“IPO”), ISS will generally issue

¹ See Institutional Shareholder Services Inc., [2017 Benchmark Policy Consultation](#).

adverse vote recommendations for individual directors, committee members, or the entire board, taking several enumerated factors into consideration. Among these factors is “[a] commitment to put the provision to a shareholder vote within three years of the date” of the IPO. As with “established” companies, in the case of newly public companies, ISS takes a case-by-case approach on director nominees in subsequent years, unless the provision is reversed or ratified by a shareholder vote.

This year, ISS proposes to make two key changes to its proxy voting policy on unilateral board actions. First, ISS proposes to issue adverse director recommendations when a company completes its IPO “with a multi-class capital structure in which the classes do not have identical voting rights.” Second, ISS proposes to remove, from its current policy, “references to putting adverse provisions to a shareholder vote as an evaluation factor for director recommendations.” Instead, ISS proposes to consider only “the inclusion of a reasonable sunset provision on the adverse capital structure or governance provisions.”

2. Restrictions on Shareholders’ Ability to Amend Bylaws

Noting that “[s]hareholders’ ability to amend the bylaws is considered a fundamental right,” ISS proposes to adopt a new policy that provides that it will recommend a vote against or withhold from members of the governance committee, on an ongoing basis, if the company’s “charter or articles of incorporation impose undue restrictions on shareholders’ ability to amend the bylaws.” According to ISS, among such restrictions are:

- outright prohibition on the submission of binding shareholder proposals; and
- share ownership requirements or time holding requirements in excess of Rule 14a-8 under the Securities Exchange Act of 1934.²

3. General Share Issuance Proposals (Cross-Market Companies)

In certain jurisdictions outside the U.S., corporate law requires shareholder approval for any share issuances. According to ISS, “companies in these markets typically seek approval every year for a general mandate for share issuances in the coming year, up to a specified percentage of issued share capital.” For companies listed in the U.S. but incorporated outside the U.S., ISS currently evaluates share issuance proposals under the policy of the company’s country of incorporation (most commonly, ISS’s proxy voting policy for the U.K. and Ireland or Continental Europe). According to ISS, however, “those policies are often driven by local listing rules and best practices, which do not generally apply to companies without a listing in that market,” and companies listed in the U.S. are subject to stock exchange listing requirements of the New York Stock Exchange or Nasdaq regarding share issuances, which are not reflected in ISS’s non-U.S. policies. Accordingly, ISS proposes to adopt a new policy on general share issuance proposals for companies listed in

² Rule 14a-8 provides that any shareholder that has continuously held at least \$2,000 in market value, or 1%, of the company’s securities for at least one year is eligible to submit a shareholder proposal.

the U.S. but incorporated outside the U.S. Specifically, ISS's U.S. policy "would recommend in favor of general share issuance authorities (i.e., those without a specified purpose) up to a maximum of 20 percent of currently issued capital, as long as the duration of the authority is clearly disclosed and reasonable."³

As indicated by ISS, share issuance proposals at dual-listed companies that are required to comply with listing rules in the country of incorporation would continue to be evaluated under the policy for that market.

4. Executive Pay Assessments (Cross-Market Companies)

Companies listed in the U.S. but incorporated in a different country may be required to include, on the same ballot, several compensation proposals relating to the same pay program (e.g., a say-on-pay advisory vote required under U.S. and U.K. law and a forward-looking binding vote on remuneration policy, mandated only by U.K. law). Under ISS's current approach, "items that are on the ballot solely due to the requirements of another market (listing, incorporation, or national code) may be evaluated under the policy of the relevant market, regardless of the 'assigned' market coverage." ISS now proposes to adopt a policy, applicable only to U.S. domestic issuers, indicating that where such issuers have multiple compensation proposals on the ballot pertaining to the same program, such proposals will be assessed on a case-by-case basis using two guiding principles:

- ISS will "align voting recommendations so as to not have inconsistent recommendations on the same pay program"; and
- ISS will "use the policy perspective of the country in which the company is listed (e.g., U.S. say-on-pay policy for proposals relating to executive pay)."

In cases in which a compensation proposal on the ballot does not have an applicable U.S. policy, ISS would apply the policy for the country that requires the proposal to be on the ballot. According to ISS, however, this is "a limited carve out."

³ While the language of ISS's proposed policy suggests that the policy would apply to share issuance proposals, some are speculating that the principal effect of ISS's proposed policy, at least from an Irish/United Kingdom perspective, would be to increase the permissible threshold of issued share capital for cash without preemption rights from 5% to 20%.

If you have any questions or would like additional information, please do not hesitate to contact **Yafit Cohn** at +1-212-455-3815 or yafit.cohn@stblaw.com, or any other member of the Firm's Public Company Advisory Practice.

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