



ISS Issues FAQs on Director Qualification Bylaws

January 22, 2014

On January 13, 2014, Institutional Shareholder Services (“ISS”) issued [FAQs](#) detailing its position on adopted or proposed bylaws that disqualify any director nominee who receives third-party compensation (“director qualification bylaws”). This guidance implicitly recognizes and addresses a trend among certain activist institutional investors to offer a special compensation arrangement to their slate of director nominees and comes on the heels of last year’s bitter proxy fight between Hess Corp. and its institutional investor, Elliott Management Corp., in which Elliott offered a bonus scheme to its director nominees, tied to Hess’s short-term performance.

ISS articulated the following guidance with regard to director qualification bylaws:

- Board’s adoption of director qualification bylaw without shareholder vote: ISS clarified its position that a board’s unilateral adoption of a bylaw disqualifying director nominees receiving third-party compensation “may be considered a material failure of governance because the ability to elect directors is a fundamental shareholder right.” ISS indicated that in accordance with its “Governance Failures” policy, it may, in such a case, recommend a vote against or withhold from director nominees. ISS noted, however, that it has not recommended voting against directors and boards adopting a bylaw, without shareholder approval, prohibiting board service by a director nominee who *fails to disclose* third-party compensation. ISS reasoned that such a bylaw “may provide greater transparency for shareholders, and allow for better-informed voting decisions.”
- Director qualification bylaw put to shareholder vote: Where a board puts a director qualification bylaw to a shareholder vote, ISS stated that it will determine on a case-by-case basis whether to recommend in favor of the proposed bylaw. Factors weighed by ISS in its analysis include, but are not limited to: (1) the board’s rationale for proposing the bylaw; (2) whether the proposed bylaw materially impairs shareholder rights; and (3) market-specific practices or views on the issue.

ISS also addressed its evaluation of director nominees with third-party compensation arrangements who are involved in a proxy contest, mentioning briefly that “[c]ompensation arrangements with director nominees are among the factors ISS considers” in its “case-by-case analysis of proxy contests.”

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

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