

Publications

Securities Alert: ISS Issues 2019 Proxy Voting Guidelines Updates

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On November 19, 2018, Institutional Shareholder Services Inc. (ISS) released updates to its proxy voting guidelines for 2019 (2019 Updates). The 2019 Updates are effective for shareholder meetings on or after February 1, 2019. This alert summarizes the key highlights of the 2019 Updates.

Board Gender Diversity

For 2019 meetings of shareholders, ISS will not make an adverse vote recommendation with respect to any director nominees in uncontested elections due to a lack of gender diversity on the company's board of directors.

However, **for 2020 meetings of shareholders of companies in the Russell 3000 or S&P 1500**, ISS will generally vote against or withhold from the chair of the nominating committee (or other directors on a case-by-case basis) if there are no women on the company's board of directors. Mitigating factors will include: (1) a firm commitment, as stated in the proxy statement, to appoint at least one female to the board in the near term; (2) the presence of a woman on the board at the preceding annual meeting; or (3) other relevant factors as applicable.

Board Attendance

ISS has generally recommended a vote against/withhold from a director who attends less than 75 percent of the aggregate of their board and committee meetings for the period for which the director served, unless the company discloses an acceptable reason for the director's absences in an SEC filing.

Under the 2019 Updates, in cases of chronic poor attendance without reasonable justification, ISS will also generally recommend a vote against/withhold from appropriate members of the company's nominating and governance committee or full board. ISS defines "chronic poor attendance" as three or more consecutive years of poor attendance without reasonable explanation or a long-term pattern of

absenteeism (e.g., poor attendance the previous year and three out of the four prior years). ISS will apply the updated policy as follows: (1) after three years of poor attendance by a director, recommend a vote against/withhold from the chair of the nominating or governance committee; (2) after four years, recommend a vote against/withhold from the full nominating and governance committee; and (3) after five years, recommend a vote against/withhold from all nominees.

Use of Economic Value Added Measures in CEO Pay-for-Performance Methodology

Proxy research reports issued by ISS in 2019 will feature Economic Value Added (EVA) measures as a supplement to the unadjusted GAAP measures used in its Financial Performance Assessment for evaluating the alignment between CEO and company performance. ISS indicated that it will consider directly including EVA measures as part of the Financial Performance Assessment in 2020.

Management Proposals to Ratify Existing Charter or Bylaw Provisions

The SEC has granted grant no-action relief to certain companies that sought to exclude shareholder proposals from their ballots by including a conflicting management proposal to ratify one or more of the company's existing governance provisions. As a result, the use of management proposals to ratify existing charter or bylaw provisions increased significantly during the 2018 proxy season, apparently to block shareholder proposals that requested more shareholder-friendly governance provisions from appearing on ballots.

In response to this trend, the 2019 Updates provide that ISS may recommend a vote against/withhold from individual directors, members of the nominating and governance committee or the full board, where boards ask shareholders to ratify existing charter or bylaw provisions based on various considerations, including, among others: (1) the presence of a shareholder proposal addressing the same issue on the same ballot; (2) the board's rationale for seeking ratification; (3) the history of management and shareholder proposals on the provision at the company's past meetings; (4) whether the current provision was adopted in response to the shareholder proposal; and (5) previous use of ratification proposals to exclude shareholder proposals.

In addition, the 2019 Updates include a new policy pursuant to which ISS will generally vote against management proposals to ratify provisions of the company's existing charter or bylaws, unless the governance provisions align with best practice.

Finally, the 2019 Updates provide that ISS will vote on a case-by-case basis on individual directors, committee members or the entire board of directors, as appropriate, if the board failed to act on a management proposal seeking to ratify an existing charter or bylaw provision that received opposition of a majority of the shares cast in the previous year.

Director Performance Evaluation

The 2019 Updates modify the company performance element of the ISS director performance evaluation methodology by (1) applying the five-year total shareholder return component to Russell 3000 companies during the initial screen instead of as a part of the secondary step in the analysis and (2) removing the five-

year total shareholder return component from the ISS director performance evaluation methodology applicable to companies not included in the Russell 3000.

Environmental and Social Shareholder Proposals

The 2019 Updates clarify that ISS will evaluate environmental and social proposals primarily on the basis of whether the proposal is likely to enhance or protect shareholder value. The 2019 Updates also supplement the list of additional factors considered by ISS in its evaluation of environmental and social proposals to include whether there are significant controversies, fines, penalties or litigation associated with the company's environmental or social practices.

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