Business Roundtable

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BY EMAIL

Global Policy Board
Institutional Shareholder Services Inc.
702 King Farm Boulevard, Suite 400
Rockville, MD 20850

Dear Ladies and Gentlemen:

Re: 2015 Proposed Voting Policy on "Independent Chair Shareholder Proposals (U.S.)"

This letter is submitted on behalf of Business Roundtable, an association of chief executive officers of leading U.S. companies working to promote sound public policy and a thriving U.S. economy. Business Roundtable's CEO members lead U.S. companies with $7.4 trillion in annual revenues and more than 16 million employees. Business Roundtable member companies comprise more than a third of the total value of the U.S. stock market and invest $158 billion annually in research and development—equal to 62 percent of U.S. private R&D spending. Our companies pay more than $200 billion in dividends to shareholders and generate more than $540 billion in sales for small and medium-sized businesses annually. Business Roundtable companies give more than $9 billion a year in combined charitable contributions.

Business Roundtable appreciates the opportunity to participate in the annual process that Institutional Shareholder Services (ISS) uses to formulate its proxy voting policies, and we welcome the ability to comment on one of the changes that ISS is considering for 2015 on its policy relating to independent chair shareholder proposals. The changes ostensibly incorporate additional flexibility into the process that ISS will use in deciding whether to support these proposals by adding to the list of factors that ISS considers and providing for the evaluation of "all of the factors in a holistic manner." However, we believe ISS should exercise considerable restraint in substituting its judgment on how a public company board structures itself over the judgment of the Board that is in a far better position to make these judgments. Also unlike ISS, the Board has fiduciary duties in connection with making these judgments.

Further, we have concerns that, in practice, these changes will result in a one-size-fits-all voting policy that promotes the adoption of an independent chair model at all companies under all circumstances. We do not believe that it is appropriate for ISS to take on the role of prescribing specific governance practices, particularly where the practice would apply indiscriminately to all companies and the benefits of the practice have failed to receive widespread recognition, which is the case with independent chairs.

Business Roundtable has long recognized the importance of allowing individual companies, and their boards of directors, the flexibility to determine the corporate governance practices that are most appropriate for them. In this regard, we believe that there is no one approach to corporate governance that is suitable for all companies, as noted in our *Principles of Corporate Governance (2012)*, a set of guiding principles intended to assist corporate boards of directors and management in their individual efforts to implement best practices of corporate governance.

In the context of board leadership, Business Roundtable believes that independent board leadership is critical to effective corporate governance, as we state in our *Principles of Corporate Governance (2012)*. However, there are different ways to accomplish this. As discussed in the *Principles*, no one leadership structure is right for every corporation at all times, and boards of different corporations may reach different conclusions about the leadership structures that are most appropriate for their corporations at any particular point in time. For example, when a CEO steps down, the board may determine that there are reasons for that person to continue in the role of chairman, such as maintaining relationships with significant customers or regulators, or deep knowledge of the company's industry.

Given the different circumstances that companies may face, we believe that decisions about the optimal leadership structure for a company's board of directors are matters of business judgment for the board and therefore, most appropriately left to the board itself. Directors have a legal obligation to exercise informed, independent judgment to make decisions that are in the best interests of the corporation and its shareholders. Accordingly, as discussed in the *Principles of Corporate Governance (2012)*, each board should evaluate whether to separate the positions of chairman and CEO or combine them, based on the board's assessment of what is in the best interests of the company and its shareholders, considering the company's particular circumstances. Additionally, the board should consider the appropriate leadership structure each year, as part of the CEO succession planning process. Finally, if the board combines the roles of CEO and chairman or has a chairman who is not independent, the board should appoint a lead director to provide independent leadership for the board.

Allowing flexibility in board leadership structures is consistent with the approaches of major institutional investors such as State Street Global Advisors (SSgA) and BlackRock. SSgA analyzes independent chair shareholder proposals on a case-by-case basis, taking into consideration a variety of factors including a company's performance and governance structure.[1] Similarly, while BlackRock "believe[s] that independent leadership is important in the board room," it generally considers the designation of a "strong" lead director "as an acceptable alternative to an independent chair."[2]

With respect to the role of lead directors, in the release discussing the proposed voting policy for 2015, ISS states that "it is debatable whether a lead independent director can act as an effective counterbalance to both a CEO and an executive chair." It is not clear to us on what basis ISS makes such a strong statement that serves as an important justification for its policy change. Further, the release also states that when ISS assessed the potential impact of the proposed policy the assessment resulted in "a higher level of support" for independent chair shareholder proposals. Based on this, Business Roundtable has serious concerns that, although the policy purports to allow for greater consideration of company-specific factors, it in fact reflects a blanket preference for an independent chair structure.

We strongly believe that it is inappropriate for ISS to establish governance standards, particularly in areas where the merits of a particular governance practice are not widely accepted or supported by empirical evidence. Significantly, studies on board leadership structure show a pronounced lack of consensus about the impact of appointing an independent chairman. According to a 2013 study that surveyed two decades of prior studies on the subject, a "stream of research . . . has shown, fairly conclusively, that CEO duality [the assignment of CEO and board chair roles to one individual] has no substantive, systematic relationship with firm performance."[3] The study went on to note that "the lack of an evident relationship between board leadership structure and firm performance exhibits 'a level of consistency . . . unusual in any literature'."[4] Similarly, according to Harvard Law School Professor John Coates, the "only clear lesson" from over 34 studies conducted over a 20-year period, of differences in performance between companies with combined and separate chairman/CEO roles, is "that there has been no long-term trend or convergence on a split chair/CEO structure, and that variation in board leadership structure has persisted for decades, even in the UK, where a split chair/CEO structure is the norm."[5]

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1 State Street Global Advisors, *Proxy Voting and Engagement Guidelines—US*, at 4 (March 2014).

2 BlackRock, *Proxy Voting Guidelines for U.S. Securities*, at 6 (April 2014).

3 Ryan Krause & Matthew Semadeni, *Apprentice, Departure, and Demotion: An Examination of the Three Types of CEO-Board Chair Separation*, Academy of Management Journal, Vol. 56, No. 3, 805, at 807 (June 2013) (citations omitted).

4 *Id*. (citation omitted).

5 Testimony of Professor John C. Coates IV, John F. Cogan, Jr. Professor of Law and Economics, Harvard Law School, Before the Subcommittee on Securities, Insurance, and Investment of the United States Senate Committee on Banking, Housing, and Urban Affairs, Hearing on Protecting Shareholders and Enhancing Public Confidence by Improving Corporate Governance, §B.b (July 29, 2009).

For these reasons, Business Roundtable believes that ISS should accord substantial deference to the determination that a company's board of directors has made about the board leadership structure that is most appropriate for the company at any particular time and that the board's rationale for employing a particular leadership structure is a significant factor ISS should consider in evaluating independent chair shareholder proposals. Under Securities and Exchange Commission rules, companies must provide disclosure about their board leadership structures in the annual proxy statement, including disclosure about why a company has determined that its leadership structure is appropriate given its specific characteristics or circumstances. This factor should be given significant weight when ISS formulates voting recommendations because it is the responsibility of a company's board of directors to determine the appropriate leadership structure for the board, in the exercise of the board's business judgment and consistent with the directors' fiduciary duties to the company and its shareholders. Implementing ISS's stated goal of evaluating independent chair shareholder proposals by looking at a host of company-specific factors "in a holistic manner" requires meaningful consideration of companies' individual circumstances, including—and most importantly—the board's reasons for choosing the leadership structure that it has in place at the time of the shareholder proposal.

Thank you for considering our comments as part of the 2015 policy formulation process. Please do not hesitate to contact Michael J. Ryan, Jr., of the Business Roundtable at (202) 496-3275 or mryan@brt.org, if we can provide further information.

Sincerely,

Alexander M. Cutler
Chairman and Chief Executive Officer
Eaton
Chair, Corporate Governance Committee
Business Roundtable

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