Center On Executive Compensation

October 29, 2014

VIA EMAIL

Dr. Martha Carter
Chair
Global Policy Board
Institutional Shareholder Services, Inc.
2099 Gaither Road
Rockville, MD 20850-4045

RE: Center On Executive Compensation Comments in Response to 2015 Draft ISS Policy Changes

Dear Dr. Carter:

The Center On Executive Compensation ("Center") is pleased to submit its comments on Institutional Shareholder Services, Inc.'s ("ISS") 2015 draft policies on behalf of its Subscribers.

As you know, the Center is a research and advocacy organization that seeks to provide a principles-based approach to executive compensation policy from the perspective of the senior human resource officers of leading companies. The Center is a division of HR Policy Association, which represents the chief human resource officers of over 360 large companies, and the Center's more than 100 subscribing companies are HR Policy members that represent a broad cross-section of industries. Because senior human resource officers play an important role in supporting the compensation committee, we believe that our Subscribers' views are particularly helpful in better understanding how executive compensation plans are developed and executed, especially in the era of say on pay.

Consistent with the Center's mission, our comments are focused on ISS's policy changes regarding the new equity plan scorecard.

New Equity Plan Scorecard

In its proposed 2015 policies, ISS indicated that it plans to adopt a new "scorecard" model for evaluating equity plan proposals that will take into account a variety of factors around cost, plan features and grant practices using a more qualitative approach than previously. ISS has noted that this means that rather than relying on a set of pass/fail tests to determine a vote recommendation for equity plan proposals, the new model will allow a range of factors to be evaluated holistically so that more quantitative aspects of the plan such as cost may be mitigated or outweighed by more qualitative aspects such as vesting requirements or proportion of performance-based pay. ISS has specifically sought comment on any unintended consequences of shifting to a scorecard approach.

The Center appreciates the attempt to create a more nuanced evaluation methodology for equity plan proposals. However, we continue to have concerns that this approach may result in less flexibility for companies with regard to their use of equity awards, since the evaluation of equity plans may be disproportionately affected by factors which should more properly be considered in the context of a say on pay proposal. For example, ISS has noted it will consider as a "positive" factor the presence of minimum vesting periods for awards made under the plan. Although most companies adopt vesting periods on long-term incentive awards to retain key talent and tie executives' pay to the long-term interests of shareholders, there may be situations in which the purpose of certain awards weighs in favor of using different vesting periods, such as in a new hire situation where the grant is made to make up for forfeited awards at the executive's prior firm. If the rationale for such a decision is clearly disclosed in the proxy, and the use of such awards is limited, the mere existence of an award with less than a "minimum" vesting period should not be enough to influence a vote recommendation against an equity plan proposal. However, under the scorecard as described, a shorter vesting period could be a significant negative factor in the qualitative analysis.

The Center also strongly discourages ISS from attempting to use binding equity plan vote recommendations to influence substantive plan design factors, such as vesting periods for equity awards, clawback policies, and post-vesting share-holding requirements. These are more properly considered as part of the non-binding say on pay vote evaluation and recommendation.

In addition, the Center is concerned that given the lack of detail ISS has provided regarding exactly how the various qualitative factors within the scorecard model will be weighted and considered, the new approach will essentially become a "black-box" exercise in which companies will be left with considerable uncertainty. A qualitative approach may afford ISS the flexibility to assess the context of a company's program and the factors that weigh in favor or against supporting an equity plan. However, based on some of our Subscribers' experiences with ISS's qualitative analysis in the pay for performance context, there is also concern that ISS will be inconsistent in how they assess the equity plan factors from company to company. As has happened in the pay for performance context, this approach may drive companies to conform their equity plans to ISS's list of "do's and don'ts," rather than adopt a tailored approach that best serves individual companies and their shareholders. It may also lead companies to see consulting services from ISS's consulting arm when they would not ordinarily do so. The Center suggests that in ISS's final policy release, the criteria employed for evaluating equity plan proposals should be as transparent as possible, including what weightings will be used and which plan factors will figure most heavily in the overall evaluations and vote recommendations.

Conclusion

The Center On Executive Compensation appreciates the opportunity to submit its views on the 2015 policy process and welcomes the chance to provide the corporate perspective on ISS's policies. Please do not hesitate to contact Ani Huang at ahuang@execcomp.org or 202-315-5531, if you have any questions about our comments or would like to discuss them further.

Sincerely,

Timothy J. Bartl

Timothy J. Bartl
President