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October 28, 2014

Mr. Gary Retelny
President
Institutional Shareholder Services
702 King Farm Boulevard
Suite 400
Rockville, MD 20850

Sent via email to: Policy@ISSGovernance.com

Re: 2015 Benchmark Policy Consultation

Dear Mr. Retelny:

The U.S. Chamber of Commerce ("Chamber") is the world's largest business federation, representing more than 3 million businesses and organizations of every size, sector, and region. The Chamber created the Center for Capital Markets Competitiveness ("CCMC") to promote a modern and effective regulatory structure for capital markets to function fully and properly in a 21st century economy. In furtherance of this objective, a chief priority of the CCMC is to advance an accountable and transparent corporate governance regime. The CCMC appreciates this opportunity to comment on Institutional Shareholder Services Inc.'s ("ISS") 2015 Benchmark Policy Consultation ("Consultation").[1] Our comments are directed to the Consultation Policies stated to be applicable solely to U.S.-based companies.[2]

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[1] *See* ISS, 2015 Benchmark Policy Consultation, available at https://www.issgovernance.com/policy-gateway/2015-benchmark-policy-consultation/?doing_wp_cron=1413832126.6937229633331298828125.

[2] These questions include independent chair shareholder proposals, available at https://www.issgovernance.com/file/publications/independent-chair-shareholder-proposals-us.pdf, and ISS' proposed equity plan scorecard, available at https://www.issgovernance.com/file/publications/equity-plan-scorecard-us.pdf.

The CCMC is concerned that the "Policy Consultation" is not really a consultation at all—it was published on October 15, 2014, but requires a response no later than 6 pm on October 29, 2014. The issues raised vis-à-vis U.S.-domiciled companies are complex, and ISS' abbreviated descriptions of them do not lend them to instant analysis, given the abbreviated time frame provided. Utilizing a time frame this compact strongly suggests the outcome of this "Consultation" is already known, and that the "Consultation" reflects a decision in search of a process.

Similarly, the CCMC is concerned that the policies briefly articulated in the Policy Consultation lack a foundation based on empirical facts, well known to the companies to which these new standards will be applied. Finally, even though the Policy Consultation purports to be applying a company-by-company analysis, in fact the judgments contemplated would merely mask the basis for any ISS recommendation, and remove the only certainty in the existing rules—to wit, the limited circumstances under which ISS would recommend a favorable vote.[3]

Independent Chair Shareholder Proposals

While we commend ISS for its stated goal of predicating its recommendations regarding independent chair shareholder proposals on "a holistic review of each company's board leadership structure, governance practices, and financial performance,"[4] this issue is a complicated one, and ISS itself concedes that, despite its reference to a "holistic review," the likely result of the new proposed policies will be

[3] In recent guidance to investment portfolio management organizations ("IPMOs") and proxy advisory firms ("PAFs"), the SEC Staff emphasized the need for clients of PAFs to understand the factual and empirical bases for recommendations, to exercise their fiduciary obligations not to accept PAF recommendations at face value, and to monitor recommendations for factual errors and out-of-date information. *See SEC Staff, Legal Bulletin No. 20* (June 30, 2014), at Questions 3 and 4, available at http://www.sec.gov/interps/legal/cfslb20.htm. The nature of the proposed changes ISS is considering would make this extremely difficult, if not impossible, for IPMO clients to achieve.

[4] *See* "*Independent Chair Shareholder Proposals,*" *supra* n. 2, at p. 2.

to produce "a higher level of support for the resolutions,"[5] accompanied by far less clarity about the reasons that ISS will support more of these shareholder resolutions.[6]

Under ISS' revised policy, according to the Consultation, "any single factor that may have previously resulted in a 'For' or 'Against' recommendation may be mitigated by other positive or negative aspects, respectively."[7] Of course, there is no delineation of what these "other positive or negative aspects" may be, how they would be weighted, or how they would be applied. This leaves public companies as well as ISS' clients at sea as to what prompted a determination that previously would have seen ISS oppose more of these proposals.[8] This is a change that would, if enacted, fly in the face of explicit SEC Staff Guidance on the obligations to verify the accuracy and current nature of information utilized in formulating voting recommendations.[9]

The proposed new policy—as yet undefined and undisclosed—is also lacking in any foundation of empirical support. As has recently been observed, "[n]either the empirical data nor corporate governance theory support requiring companies to have a non-executive chairman."[10] Indeed, a number of studies confirm that there is no empirical support for or against the proposition ISS seems eager to adopt.[11]

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[5] *Id.*

[6] *See*, *e.g.*, S. Bainbridge, ProfessorBainbridge.com, "*Comment on the 2015 Benchmark Policy Consultation re Independent Chair Shareholder Proposals*" (Oct. 17, 2014) ("Prof. Bainbridge ISS Comments"), http://www.professorbainbridge.com/professorbainbridgecom/corporate-law/ ("The effect of [the proposed] change would be to make it even more difficult for companies to obtain an ISS recommendation against such proposals").

[7] *See* "*Independent Chair Shareholder Proposals*," *supra* n. 2, at p. 2.

[8] The description of the proposed changes merely states that ISS will add "new governance, board leadership, and performance factors to the analytical framework. . . . Notably, the policy update would add new factors that are not considered under the current policy including the absence/presence of an executive chair, recent board and executive leadership transitions at the company, director/CEO tenure, and a longer (five-year) TSR performance period." *Id.* There is no indication of what these factors actually are, or how they would be applied, or whether they would be viewed as positive or negative, and why.

[9] *See* n. 3, *supra*.

[10] *See Prof. Bainbridge ISS Comments*, *supra* n. 6.

[11] *See*, *e.g.*, O. Faleye, "*Does One Hat Fit All? The Case of Corporate Leadership Structure*," 11 Jl. Of Mgmt. & Gov. 239 (2007), available at http://web.cba.neu.edu/~ofaleye/doc/hats.pdf (companies actively weigh costs and benefits of alternative leadership structures, based on their unique circumstances, so one-size-fits-all is counter productive); J. Brickley, J. Coles, G. Jarrell, "*Leadership Structure: Separating the CEO and Chairman of the Board*," 3 Jl. Corp. Fin. 189 (1997), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=6124 (paucity of evidence available to suggest that combining or

Ironically, the Consultation's request for comments seeks exactly the kind of information that ISS declines to provide in seeking informative comments. Thus, for example, ISS solicits specific information on the precise "factors" each respondent considers most important in determining whether an independent chair shareholder proposal warrants support.[12] Without indicating the factors ISS considers most important, the Policy Consultation severely hampers the ability of interested persons to comment effectively on this change. Indeed, the failure to provide this information suggests that the implementation of this new policy is premature—it does not appear to be a policy fully formulated, begging the question why it is so critical for ISS to implement these changes *now*, and provide such a short timeframe for public comment.

Of a similar nature is the second of the three questions on which ISS seeks specific feedback in its Policy Consultation—the "weight... [given] to recent changes in board leadership structure."[13] In posing this question, ISS insists upon receiving specificity from those who respond to this Consultation as to "issues and relative weights."[14] Again, these are details notably missing from ISS' Consultation, but absolutely essential to obtain meaningful commentary and analysis, all of which suggests that:

- The actual substance of the new Policy is still being formulated;
- Even when formulated, the new Policy will not be provided with great specificity or clarity; and

separating Chairman and CEO titles has any effect on corporate performance); Prof. J. Coates, "*Protecting Shareholders and Enhancing Public Confidence through Corporate Governance*," Harv. L. School Forum on Corp. Gov. & Fin. Reg, (July 29, 2009) (summarizing Congressional testimony demonstrating that 34 studies of the effect of corporate governance structure yield precious little in the way of empirical data to support any single outcome), available at http://blogs.law.harvard.edu/corpgov/2009/07/30/protecting-shareholders-and-enhancing-public-confidence-through-corporate-governance/.

[12] *See* "*Independent Chair Shareholder Proposals,*" *supra* n. 2, at p. 2.

[13] *Id.*

[14] *Id.*

- Comments on ISS' precatory proposals are unlikely to effectively demonstrate the need for changes in ISS' ultimate policy decisions, especially since those ultimate policy decisions will not be known at the time comments are submitted.[15]

ISS should be concerned that its adoption of a new approach to important governance issues, if not thoroughly and effectively communicated to public companies and the investing public—and that certainly would be the case here—will foster uncertainty that ultimately benefits ISS' corporate consulting business at the expense of companies and their shareholders.[16] If this is not ISS' intention, it should take all reasonable steps to avoid conveying the appearance that this is, in fact, ISS' actual intention.

<u>Equity Plan Scorecard</u>

The proposed "Consultation" on potential changes to ISS' policies on its equity plan scorecard is stated to be for the purpose of achieving a "more nuanced approach around traditional cost evaluation."[17] But, while a balanced scorecard approach makes great sense, there is no clear indication on the part of ISS as to what weight it will assign to each category of assessment—cost of plan, plan features, and company grant practices. Indeed, one of the specific questions posed by ISS in its Consultation is whether certain factors should be more heavily weighted, and if so, to what extent.[18]

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[15] Remarkably, the solicitation of comments on the proposed Equity Plan Scorecard contains greater specificity regarding the standards to be considered and the weight to be accorded to them than is present in the solicitation relating to independent chair shareholder proposals. *See Equity Plan Scorecard*, *supra* n. 2, at p. 2.

[16] We have previously raised this issue for ISS' consideration. *See* CCMC Letter to ISS, Re: 2015 ISS Policy Survey (Sept. 2, 2014), at p. 12, available at http://www.centerforcapitalmarkets.com/wp-content/uploads/2014/09/2014-9.2-ISS-Survey-Letter-.pdf.

[17] *Id.*

[18] *See Equity Plan Scorecard*, *supra* n. 2, at p. 3.

Again, this suggests that ISS intends to weight the factors it identifies, but is unwilling or unable to specify which factors will be entitled to what weight.[19]

As noted above with respect to independent chair shareholder proposals, this approach benefits ISS (and in particular its' consulting operations), but does nothing to advance either corporate or shareholder interests or benefits. The Consultation also makes clear that, for all ISS' purported interest in creating a more "nuanced" approach, in fact the proposed policy fosters a one-size-fits-all system that fails to take into account the different unique needs of companies and their investors. Thus, for example, ISS specifically acknowledges that factors ***it*** considers "highly egregious," will "continue to result in negative recommendations regardless of other factors."[20]

We believe that these inherent flaws in the Consultation can adversely affect harm companies and their shareholders. In its questions, ISS specifically requests input on whether there are any "unintended" consequences from moving to the proposed scorecard approach. We cannot say whether the consequences we perceive are actually unintended or not, but even assuming they are unintended, the approach ISS is considering, adopted under severe time constraints, and without adequate data and details, surely will not advantage public companies or their investors, but certainly could produce significant advantages for ISS itself.

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CCMC appreciates this opportunity to comment on ISS' 2015 Survey. However, as discussed above, we believe the Consultation is fundamentally flawed,

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[19] *See*, *e.g.*, D. Kalfen, "*ISS 2014-2015 Policy Survey Summary of Results*" (Oct. 6, 2014), available at http://www.meridiancp.com/insights/iss-2014-2015-policy-survey-summary-of-results/ ("If ISS assigns substantial weight to the plan features category, then the balanced scorecard approach would likely introduce a significant lack of predictability and clarity to ISS's evaluation process for equity plan proposals").
[20] *See Equity Plan Scorecard*, *supra* n. 2, at p. 2.

since—among other things—it seeks to elicit opinions with a very short timeframe for response, based on inadequate disclosure of the actual policies being contemplated, in the absence of any empirical data demonstrating a nexus to improving shareholder value, all without any explanation—or apparent rationale—for the rushed environment in which these issues are forcibly being considered. Particularly given the SEC Staff's recent guidance, this entire approach makes even less sense than it otherwise would. Proxy votes cast in reliance on proxy voting policies based upon this Consultation cannot—by definition—be reasonably designed to further shareholder values. We would be happy to discuss the issues raised in this letter with you or the appropriate staff of ISS, if you would find that helpful.

Sincerely,

Tom Quaadman