

Meridian Client Update

ISS Issues New Policy on Proxy Access Proposals

On February 19, 2015, Institutional Shareholder Services (ISS) issued a revised policy on evaluating shareholder and management proposals on “proxy access.” Under the revised policy, generally ISS will support a proxy access proposal that meets certain minimum requirements (these requirements are similar to the requirements in the Securities and Exchange Commission’s (SEC’s) proxy access rule that was ultimately struck down by a federal court).

Policy on Proxy Access Proposals

ISS is proposing to implement a new method for evaluating proxy access proposals.

Prior Policy

Under its prior policy, ISS voted case-by-case on proxy access proposals, taking into account the following factors:

- Company-specific factors, and
- Proposal-specific factors, including:
 - The ownership thresholds proposed in the resolution (i.e., the percentage and duration),
 - The maximum proportion of directors that shareholders may nominate each year, and
 - The method of determining which nominees should appear on the ballot if multiple shareholders submit nominations.

ISS’s prior policy did not include any specific benchmark levels with regard to the foregoing factors.

New Policy

Under its new policy, ISS will generally recommend FOR a management or shareholder proposal on proxy access if the proposal meets the following requirements:

- Minimal or no limits on the number of shareholders permitted to form a single nominating group
- Share ownership requirement may not exceed 3% of the outstanding voting securities
- Share holding requirement may not exceed 3 continuous years for each member of a nominating group
- Cap on the number of board nominees of generally 25% of the full board

If a proxy access proposal sets forth criteria that is more restrictive than the guidelines above, then ISS will generally recommend a vote AGAINST the proposal. ISS will also review the reasonableness of any other restrictions on the right of proxy access in determining whether to support a proxy access proposal.

For companies that present both a management and a shareholder proxy access proposal on the ballot, ISS will review each proposal separately under its policy.

Management Exclusion of Shareholder Proxy Access Proposal

Under its new policy on proxy access, ISS also will consider management’s exclusion of a shareholder proposal on proxy access to be a “governance failure” negatively affecting its vote recommendation on board members, except in certain limited circumstances as described below.

ISS will generally recommend a vote AGAINST one or more directors, if a company omits from its corporate ballot a properly submitted shareholder proxy access proposal, unless the company has obtained:

- Voluntary withdrawal of the proposal by the proponent,
- No-action relief from the SEC, or
- A U.S. District Court ruling that the company may exclude the proposal from its proxy ballot.

ISS may recommend a vote AGAINST individual directors, certain committee members or the entire board dependent on the company-specific facts and circumstances.

An ISS vote recommendation AGAINST directors would occur regardless of whether a management-sponsored proxy access proposal appeared on the same ballot.

If a company has taken unilateral steps to implement a shareholder proxy proposal, however, the degree to which the proposal is implemented and any additional material restrictions on the right to proxy access will factor into ISS’s vote recommendation on directors.

Meridian comment. We may be at a turning point with regard to proxy access. Several large and high-profile companies have already adopted proxy access or have included management-sponsored proxy access proposals on their corporate ballot. Companies adopting proxy access include General Electric, Verizon, CF Industries, Hewlett-Packard, Western Union, Chesapeake Energy and Nabors Industries, and Citigroup is supporting a shareholder proposal to be included on its 2015 proxy ballot. In addition, activist shareholders continue to place proxy access proposals on corporate ballots of large public companies. For example, New York City Retirement System intends to submit proxy access proposals at 75 large public companies. Finally, due to a change of direction (see discussion below), the SEC has made it much more difficult for a company to exclude a shareholder-sponsored proxy access proposal on the grounds that it would directly conflict with a company-sponsored proposal on proxy access (generally, under federal securities laws, a public company may omit a shareholder-sponsored proposal if it directly conflicts with a management-sponsored proposal).

Late last year, Whole Foods thought it could exclude a shareholder proposal on proxy access that directly conflicted with a company proposal on the same matter without raising the ire of the SEC. In December 2014, the SEC issued a no-action letter in favor of Whole Foods agreeing that the company may exclude a shareholder proposal on proxy access because it conflicted with a Whole Foods proposal. However, due to complaints from activist shareholders and others, the SEC reversed its position in mid-January 2015. At the urging of SEC Chair White, the Division of Corporation Finance announced that it will “express no views” on the application of the SEC rule permitting exclusion of conflicting proxy proposals “during this proxy season.” Accordingly, the SEC issued a subsequent letter to Whole Foods revoking its no-action

letter and expressing no view as to whether Whole Foods' proposed exclusion of a shareholder proxy access proposal is permitted under federal securities laws.

Due to the SEC's reversal on this issue, a company faces two stark alternatives in evaluating whether to exclude a shareholder proxy access proposal upon deciding to submit a competing management proposal:

- Exclude the shareholder proposal and face the heightened risk of litigation by the proponent or an SEC enforcement action, or
- Seek a declaratory judgment in federal court finding that the exclusion is permitted under federal securities laws, thereby incurring legal expenses and potentially unwanted publicity.

Whether the foregoing events are a harbinger of a substantially increased prevalence of major public companies adopting proxy access remains to be seen. However, the weight of these events clearly suggests that the push for proxy access is gaining significant near-term momentum on several fronts, especially for large cap companies.

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The *Client Update* is prepared by Meridian Compensation Partners' Technical Team led by Donald Kalfen. Questions regarding this Client Update or executive compensation technical issues may be directed to Donald Kalfen at 847-235-3605 or dkalfen@meridiancp.com.

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