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# Meridian Client Update

## ISS Releases New Corporate Governance Scoring Tool

Institutional Shareholder Services (ISS) recently announced the release of ISS QualityScore, the fourth generation of its governance-scoring tool, which replaces ISS Governance QuickScore. According to ISS, QualityScore is intended to assist investors in identifying corporate governance risk within portfolio companies. ISS has rebranded its governance scoring tool “to better reflect institutional investors’ use of the rating as a quality measure for portfolio companies”.

During the rollout of QualityScore, ISS proxy research reports published this month prior to November 24 will **not** include a company’s QualityScore scores. Starting on November 24, ISS’s proxy research reports will include a company’s QualityScore rankings and scores.

## Overview of QualityScore

Like QuickScore, QualityScore provides a single score that arguably measures a company’s level of overall corporate governance risk and separate scores on the following four categories: (i) board structure, (ii) compensation/remuneration, (iii) shareholder rights and (iv) audit and risk oversight. Each category score is based on ISS’s raw scoring of the various factors underlying each category, which is then compared to companies in the same index (e.g., Russell 3000 or S&P 500 Indices) to determine a decile rank score.

QualityScore subscribers have the ability to access and analyze the underlying data from which the scores are generated, allowing subscribers to screen portfolio companies against hundreds of corporate governance factors or perform detailed side by side comparisons of two or more companies’ data profiles.

## Updates to Scoring Methodology and New Governance Factors

ISS’s technical document on QualityScore is available at the following link:

<https://www.issgovernance.com/solutions/iss-analytics/qualityscore/#download>

The technical document provides extensive detail on changes from QuickScore3.0, scoring methodology, factors underlying each category and the standards or criteria for evaluating certain factors. According to ISS, the new methodology “remains closely aligned with ISS’s benchmark voting policies, which in turn reflect developments in trends and market practices.” **In this regard, QualityScore includes new factors related to proxy access bylaw provisions and board compensation, refreshment and diversity.**

The new governance factors under each QualityScore category are listed in the Appendix.

**Meridian Comment.** As we have said in prior client updates, ISS's QualityScore (and its predecessor governance scoring tools) is an arbitrary method for evaluating a company's governance practices that rests on its proprietary analytical foundation. This may be the reason that ISS governance risk tools have gained little to no coverage in the popular or business press. Further, we have seen little evidence that it is influencing public debate on corporate governance or pay practices.

**From an individual company perspective, it is important to note that QuickScore does not directly impact ISS vote recommendations on Say on Pay proposals, director elections or on any other matter subject to a shareholder vote.**

Despite the lack of broader visibility in the market place, corporate boards should still possess at least a high-level understanding of QualityScore given that a company's QualityScore is made available to its major investors. However, QualityScore alone should not guide board decision making but, at best, should represent no more than a single data point for possible consideration. Ultimately, a board is under a fiduciary obligation to undertake actions that are in the best interests of all shareholders, regardless of whether the board's actions conflict with QualityScore or other ISS standards.

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# Appendix – QualityScore Governance Factors

## Board Structure

- What proportion of non-executive directors has been on the board less than 6 years?
- Does the board have any mechanisms to encourage director refreshment? (*Non-scored*)
- Does the company disclose the existence of a formal CEO and key executive officer succession plan?
- What is the proportion of women on the board?
- Has the board adequately responded to low support for a management proposal?

## Shareholder Rights and Takeover Defenses

- Does the company have a fee shifting provision (i.e., a provision that provides for the shifting of litigation expenses to an unsuccessful plaintiff)?
- Does the company have an exclusive venue/forum provision (i.e., a provision that restricts shareholder litigation against the company to certain jurisdictions)?
- Does the company have a representative claim limitation or other significant litigation rights limitations?
- Can the board materially modify the company's capital structure without shareholder approval?
- What is the ownership threshold for proxy access? (*Now scored, previously incorporated in non-scored proxy access factor*)
- What is the ownership duration threshold for proxy access? (*Now scored, previously incorporated in non-scored proxy access factor*)
- What is the cap on shareholder nominees to fill board seats from proxy access? (*Now scored, previously incorporated in non-scored proxy access factor*)
- What is the aggregation limit on shareholders to form a nominating group for proxy access? (*Now scored, previously incorporated in non-scored proxy access factor*)

## Compensation

- Does the company employ at least one metric that compares its performance to a benchmark or peer group (relative performance)?

## Audit and Risk Oversight

- What is the tenure of the external auditor?