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Meridian Compensation Partners Client Update

New ISS Policy Coming to Canada in 2016?

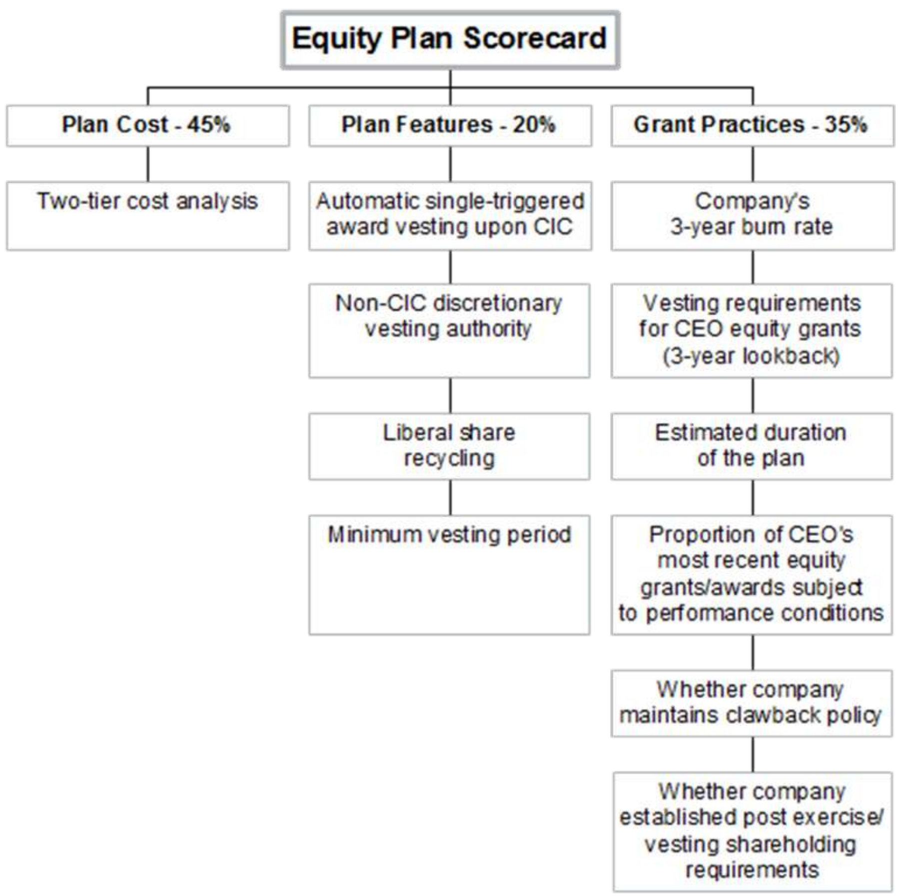
As proxy circulars are put to bed, the compensation committee's focus shifts to forward planning and understanding how the landscape is likely to change. In addition to changes in regulation, compensation committees now worry about changing proxy advisor expectations. In the United States, ISS introduced a new policy for assessing 2015 equity plan proposals. Based on past practice, we expect that ISS will expand this policy to Canadian issuers for 2016. This update provides an overview of the U.S. policy as an early indicator of what may be coming to Canada.

Overview of New U.S. Policy on Equity Plan Proposals

ISS implemented new proxy voting guidelines for U.S. equity plan proposals in 2015 proxies. Under these guidelines (the "Equity Plan Scorecard"), ISS will determine its vote recommendation on these proposals based on:

- (i) plan cost,
- (ii) plan features and
- (iii) company grant practices

Points are awarded under each of the categories, with a maximum score of 100. Generally, ISS will recommend in favour of an equity plan if a company's point score is at least 53.



Under the Equity Plan Scorecard a "positive" factor can mitigate a "negative" factor. For example, including favorable plan features (e.g., minimum vesting standards, restrictive share recycling and double-trigger vesting on a change in control) can reduce ISS concerns about equity plan costs or burn rate. Conversely, problematic practices can result in an ISS recommendation against an equity plan proposal, even when the cost of the equity plan meets ISS' requirements. For further detailed discussion on the policy features, please see our complete analysis, here.

THE REAL STORY BEHIND THE EQUITY PLAN SCORECARD and ISS'S SCORING METHODOLOGY

The Equity Plan Scorecard methodology underlies (and obfuscates to some degree) the real change in ISS's proxy voting policies on equity plan proposals. ***That is, the size of a permissible share pool is now fluid rather than fixed.*** Through a "carrot and stick" approach, ISS will increase the size of a permissible share pool if the company and its equity plan comply with ISS's proxy voting policies.

For example, we have seen ISS increase the pool by 25% where a company agreed to include minimum vesting standards. Conversely, to induce companies to ask for a smaller share pool, ISS assigns more points if the pool size is less than 65% of the ISS-determined cost benchmark.

Companies will now have to wrestle with multiple scenarios to determine the proper balance between the ISS allowable share pool and the desired plan features, with the paramount duty of boards and compensation committees being to approve plan designs and share pools that are in the best interest of shareholders and their company, whether or not this meets ISS's proxy voting policies.

Meridian comment: The full implications of ISS's Equity Plan Scorecard in the U.S. will become clearer as we move through this proxy season and any post-season feedback or changes that may result. What is already clear is that the Equity Plan Scorecard is an over-engineered and complex methodology for evaluating equity plan proposals.

While we hope that ISS works through the complexity and expected problems of the Equity Plan Scorecard before expanding it to Canada, the business benefits to ISS of selling consulting services for a scorecard this complex may result in quick implementation in the Canadian market. This raises again the issue of the apparent conflict of interest that has ISS setting the rules for its proxy voting recommendations while selling consulting services to assist issuers to meet these same provisions.

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