Arnall Golden Gregory LLP

Client Alert

Contact Attorneys Regarding This Matter:

Joseph Alley, Jr.
404.873.8688 - direct
joseph.alley@agg.com

Tanner D. Ivie
404.873.8788 - direct
tanner.ivie@agg.com

Arnall Golden Gregory LLP
Attorneys at Law

171 17th Street NW
Suite 2100
Atlanta, GA 30363-1031

1 Biscayne Tower
Suite 2690
2 South Biscayne Boulevard
Miami, FL 33131

1775 Pennsylvania Avenue NW
Suite 1000
Washington DC 20006

www.agg.com

ISS and Glass Lewis Release 2013 Policy Updates

On November 16, 2012, Institutional Shareholder Services Inc. ("ISS") released its final policy updates to its voting guidelines for the 2013 proxy season. These updates will generally be effective for shareholder meetings on or after February 1, 2013. ISS has indicated that it is holding a webcast on December 6, 2012 and releasing Frequently Asked Questions ("FAQ") in December, which will provide further discussion and elaboration on the revised guidelines.

In addition, on November 8, 2012, Glass Lewis & Co. ("Glass Lewis") released its updated voting guidelines for the 2013 proxy season. These updated guidelines will go into effect for shareholder meetings occurring after January 1, 2013. Glass Lewis previously revised its pay-for-performance model for evaluating say-on-pay proposals in July 2012.

ISS Updates

Hedging and Pledging of Company Stock: ISS now considers hedging and significant pledging of company stock by directors or executive officers as failures of risk oversight on the part of directors. Any amount of hedging will be viewed by ISS as a problematic practice warranting a negative vote recommendation. In comparison, when determining vote recommendations for election of directors of companies which currently have executives or directors with pledged company stock, ISS will take a case-by-case approach and look at the following factors: (a) presence in the company's proxy statement of an anti-pledging policy that prohibits future pledging activity; (b) magnitude of aggregate pledged shares in terms of total common shares outstanding or market value or trading volume; (c) disclosure of progress or lack thereof in reducing the magnitude of aggregate pledged shares; (d) disclosure in the proxy statement that shares subject to stock ownership and holding requirements do not include pledged company stock; and (e) other relevant factors.

Board Response to Majority Supported Shareholder Proposals: Beginning with 2014 annual meetings, ISS will start utilizing a majority of shares cast in the previous year as the sole standard for evaluating a company's response to majority supported shareholder proposals. For the 2013 proxy season, however, ISS will continue to issue a negative or withhold recommendation if the board fails to respond to a proposal that received the support of a majority of the shares outstanding in the previous year or a majority of shares cast in the last year and one of the two previous years; however, for 2013, ISS has amended its policy to allow it the flexibility to recommend against individual directors or committee members, rather than just the entire board. ISS has also provided guidance on its examination of the sufficiency of a company's action in response to a majority-supported shareholder proposal. Responding to the shareholder proposal will generally mean either full implementation of the proposal or, if the matter requires a vote by shareholders, a management proposal on the next annual ballot to implement the proposal. ISS, however, will consider, on a case-by-case basis, responses that involve less than full implementation by factoring in: (a) the proposal's subject matter; (b) the level of support and opposition provided to the resolution in past meetings; (c) disclosed shareholder outreach efforts; (d) board actions taken in response to its engagement with shareholders; (e) the continuation of the underlying issue as a voting item; and (f) other factors as appropriate.

Peer Group Methodology: ISS has modified its peer group methodology within its quantitative pay-for-performance analysis, and will now consider a company's self-selected peers' Global Industry Classification Standard ("GICS") industry group. The new methodology draws peers from the company's GICS group as well as from GICS groups represented in the company's peer group, while attempting to maintain the approximate proportions of these groups in the ISS peer group where possible. The new methodology focuses initially on the 8-digit GICS sub-industry group to identify peers that are more closely related in terms of industry. Moreover, ISS will prioritize peers that maintain the subject company near the median of the peer group, are in the subject company's peer group, and have chosen the subject company as a peer. In addition, ISS will utilize slightly relaxed size requirements, especially for very small and very large companies, and will use revenue instead of assets for certain financial companies.

Realizable Pay: As part of ISS's qualitative pay-for-performance analysis, ISS will now compare realizable pay to grant date pay, but for large capitalization companies only. Realizable pay is defined as "the sum of relevant cash and equity-based grants and awards made during a specified performance period being measured, based on equity award values for actual earned awards, or target values for ongoing awards, calculated using the stock price at the end of the performance measurement period." Stock options and stock appreciation rights, however, will be revalued, using remaining term and updated assumptions, as of the performance period, using a Black-Scholes Option Pricing model. The outcome of the realizable pay analysis may mitigate or exacerbate pay-for-performance concerns.

Voting on Golden Parachutes: The Dodd-Frank Act requires companies to hold separate shareholder votes on potential "golden parachute" payments when companies seek shareholder approval for mergers, sales, and other certain transactions. Rather than just focusing on new or extended arrangements, ISS will now consider existing change-in-control arrangements when evaluating vote recommendations for say-on-golden parachute proposals. Moreover, recent amendments that incorporate problematic features, such as excessive cash severance in excess of three times base salary and bonus, will tend to carry more weight on the overall analysis, and ISS will closely scrutinize multiple legacy problematic features in change-in-control agreements.

Social/Environmental Compensation-Related Proposals: ISS has changed its general policy of voting against proposals to link, or report on linking, compensation to sustainability (environmental and social) criteria, and will now take a case-by-case approach.

Social/Environmental Issues: ISS has adopted the overarching principle that its voting recommendations will focus on how the social and/or environmental proposal may enhance or protect shareholder value in either the short term or long term, while also considering other specific factors.

Lobbying: ISS has clarified both the scope and focus of its policy regarding proposals requesting information on a company's lobbying by adding "indirect" lobbying to the scope of the policy, and adding lobbying policies and procedures, along with activities, to the focus.

Overboarded Directors: For the purposes of determining whether a director serves on six or more public company boards, or a CEO serves on more than two public company boards in addition to the board of the company of which he is CEO, all boards of subsidiaries with publicly traded stock will now be counted by ISS as separate boards.

Categorization of Directors: ISS has amended its definition of "Inside Director" as part of an effort to simplify the categories of directors. Accordingly, the new definition of Inside Director has been expanded to include all current interim officers, not just the interim CEO, and non-executive directors named in the Summary Compensation Table. In addition, ISS will now consider director compensation as a potential impediment on director independence under the Affiliated Outside Director, rather than Inside Director, category.

Glass Lewis Updates

<u>Glass Lewis's 2013 updates include the following:</u>

Board Responsiveness: Glass Lewis has added a section to its guidelines articulating its analysis of a board's response to situations where twenty-five percent (25%) or more of shareholders "vote against" the recommendation of management. Such situations include when 25% or more of shareholders (excluding abstentions and broker non-votes) withhold votes from or vote against a director nominee, vote against a management-sponsored proposal, or vote for a shareholder proposal. Should the 25% threshold be met, Glass Lewis will closely examine the underlying issues and evaluate whether or not the board responded appropriately. As part of its evaluation, Glass Lewis will review publicly available disclosures, and will consider: (a) at the board level, any changes in directorships, committee memberships, disclosure of related party transactions, meeting attendance, or other responsibilities; (b) any revisions made to the company's governance documents; (c) any press or news releases indicating changes in, or adoption of, new company policies, business practices or special reports; and (d) any modifications made to the design and structure of the company's compensation program.

Service on Multiple Public Company Boards: The 2013 guidelines provide that when a director who serves as an executive officer of a public company also serves on more than two other public company boards, Glass Lewis will recommend a vote against that director at the other public companies where he or she serves on the board, but not at the company where the individual serves as both a director and an executive officer.

Board Committees and Committee Chairs: For 2013, Glass Lewis indicates that because the chairman of each committee bears primary responsibility for the actions of the committee, recommendations related to committee actions and performance will frequently focus on the chairman of the committee rather than on the other individuals serving on the committee. In the event that it is determined that a vote against the chairman of the committee is warranted but the chairman is not standing for election, Glass Lewis will not recommend against any of the committee members, but will express concern with regard to the committee chairman. In circumstances where there is no committee chairman or Glass Lewis is unable to determine who serves as the committee chairman, Glass Lewis will recommend voting against the longest-serving member of the committee (or the longest-serving board member if the longest-serving committee member cannot be determined).

Share Counting: In evaluating equity compensation plan proposals, Glass Lewis will consider as part of its review that "[p]lans should not count shares in ways that understate the potential dilution, or cost, to common shareholders." This refers to "inverse" full-value award multipliers.

Conclusion

As the 2013 proxy season approaches, issuers should review these changes in order to determine what actions, if any, should be taken in connection with upcoming proxy votes regarding election of directors, say-on-pay, say-on-frequency and other possible 2013 proposals.