

January 28, 2014

Alert

SEC Disclosure and Corporate Governance

ISS Announces Governance QuickScore Revamp

*Verify Your
Company's
Data Now*

Yesterday, Institutional Shareholder Services (ISS) announced a revamp of its ISS Governance QuickScore product, to be launched February 18, 2014, and the opening of its related data verification window. Information about “QuickScore 2.0,” including the revised technical document discussing the methodology and specific factors, is available at <http://www.issgovernance.com/quickscore>. ISS has added questions and so-called “zero-weight” factors that relate to, among other things, director tenure and board diversity, and has made other changes to its methodology. Companies should verify their data against QuickScore 2.0’s revised methodology by **February 7, 2014**.

Key Dates:

- January 27, 2014 – Data verification period opened
- February 7, 2014 – Deadline for verifying data (8:00 pm EST)
- February 18, 2014 – QuickScore 2.0 to be launched and reports included in ISS proxy reports
- Early March 2014 – QuickScore 2.0 reports to be available on Yahoo! Finance and Bloomberg

QuickScore 2.0 Revised Methodology – Overview

Less than a year after the launch of QuickScore 1.0, ISS has modified its QuickScore methodology to:

- Expand the number of corporate governance factors it considers when conducting “quantitative testing” of companies (discussed below)
- Better align questions with ISS voting policy and other factors
 - o For example, QuickScore 2.0’s technical document incorporates specific quantitative aspects of ISS proxy voting guidelines with respect to factors such as what it considers to be adequate stock ownership guidelines, what constitutes an “overboarded” director and various other matters; this level of detail was not included for many questions in the QuickScore 1.0 documentation
- Introduce “zero-weight” factors which highlight information about a company’s governance structures and practices that ISS is beginning to focus on, but which do not impact its QuickScore (discussed below)

- Update QuickScores on an ongoing basis using “event-driven data updates,” such as public filings that report on changes to a company’s governance structure
 - Note that ISS has stated that it will monitor Form 8-Ks and in situations where ISS “is unable to classify a director’s independence based on a company’s event-driven disclosure (e.g., appointment of a new board member), ISS will consider the director ‘unclassified’ until there is sufficient information to determine the independence classification”; “unclassified” status could potentially have a negative impact on ISS recommendations with respect to director elections and other matters, particularly where such a director serves on one of the board’s key committees
- Expand coverage in the UK and Australian markets to encompass UK Euro Stoxx and Australia ASX 200 constituents, and create a new “Australasia” region including Australian and New Zealand companies

Notwithstanding these amendments, the basic contours of the QuickScore product remain the same, as discussed in our Alert dated January 30, 2013 (available at <http://www.weil.com/articles/iss-launches-new-governance-quick-score-product-replacing-grid>).

New Factors Applicable to US Companies and “Zero-Weight” Factors

QuickScore 2.0 includes eight new factors applicable to US companies (a total of 87, up from 79 under QuickScore 1.0), some of which are zero-weight factors:

- *Director tenure* – QuickScore 2.0 considers board tenure of **more than nine years** to be “excessive”; this change reflects increasing ISS focus on board tenure, which is also a topic ISS is seeking feedback on as part of its ongoing consultation on longer-term policy changes that may impact US companies. (This consultation period ends February 14, 2014, as discussed in our Alert dated November 27, 2013, available at http://www.weil.com/~media/files/pdfs/10997_sec_iss_policy_updates_november_v5.pdf)
- *Director election results* – QuickScore 2.0 will factor in the percentage of directors who received shareholder approval rates below the industry-index level
- *Average non-employee director compensation compared with peers* – QuickScore 2.0 will factor in the average size of outside directors’ compensation as a multiple of the median of company peers; this relative measure expresses the prior year’s average outside director’s pay (based on total compensation reported for each director in the proxy statement; no exclusions are mentioned) as a multiple of the median pay of its ISS-determined peers for the same period
- *Relative degree of alignment (RDA) over a three-year period* – Reflecting recent changes to its pay-for-performance evaluation methodology for proxy voting purposes, QuickScore 2.0 will factor in the RDA between the company’s annualized three-year pay percentile rank, relative to peers, and its three-year annualized total shareholder return rank, relative to peers. (For more information on this policy change, see our Alert dated November 27, 2013 referenced above)
- *Say-on-pay results compared to industry index level* – QuickScore 2.0 will factor in whether the most recent say-on-pay proposal received shareholders’ support below the applicable industry-index level
- *New zero-weight factors:*
 - Board size – ISS considers that boards should have between 6 and 15 members, and that 9-12 members is “ideal”
 - Number/proportion of women directors – ISS does not indicate a recommended number or proportion
 - Number of audit committee financial experts – ISS does not indicate a recommended number

In addition, several factors that were considered under QuickScore 1.0 are now treated as zero-weight factors:

- Percentage of the board that consists of immediate family members of majority shareholders, executives or former

executives (within the past five years)

- Percentage of the board that consists of former or current employees of the company
- Length of any employment agreement with the CEO
- RDA pay-for-performance over three years and one year – these factors have been superseded by the RDA factor discussed above

What To Do Now?

- Provide feedback before the data verification website closes on **February 7, 2014** at 8:00 pm EST. Information about verifying data, how to obtain login information and a link to the data verification website is available at <http://www.issgovernance.com/quickscore/dataverification>. Submissions of corrected or updated data factors can be made online through the platform
 - o Companies that anticipate filing a proxy statement in the coming weeks should note that data verification is not available during the period between the filing of a company's proxy statement and the publication of ISS' proxy analysis for the company's annual meeting
 - o Data can also be verified after QuickScore 2.0 has launched on February 18, 2014
- Consider providing information about QuickScore 2.0 at the next meeting of the Nominating and Governance Committee, particularly in relation to increased ISS focus on director tenure and board diversity
- Consider whether Form 8-Ks reporting new director appointments should include more detailed disclosure with respect to independence
- As with QuickScore 1.0, companies that have adopted many of the best practices advocated by ISS may find themselves with QuickScores that are in the middle of the pack or below average, as each QuickScore will reflect a company's relative rank. Directors and management should continue to make governance decisions in the best interests of the company, depending on the company's particular circumstances, rather than be driven by a desire to increase QuickScores in line with rigid one-size-fits-all prescriptions

If you have any questions on these matters, please do not hesitate to speak to your regular contact at Weil, Gotshal & Manges LLP or to any member of Weil's Public Company Advisory Group:

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