



CLIENT ALERT

**A New Year Brings a New Methodology  
ISS Publishes Equity Plan Scorecard FAQs**

ISS recently published FAQs for its new [Equity Plan Scorecard \(EPSC\) approach for evaluating equity plan proposals](#). The methodology is effective for all U.S. companies with annual meetings on or after February 1, 2015.

**EQUITY PLAN SCORECARD METHODOLOGY**

The EPSC considers a range of positive and negative factors related to a company’s equity plan. ISS voting recommendations are based on a company’s total EPSC score. A score of 53 (out of 100 maximum total points) is required to receive a positive voting recommendation. However, ISS maintains the ability to recommend against a company, even in instances where it passes the EPSC tests, if any of the following apply:

- Awards may vest in connection with a liberal change in control definition
- The plan permits repricing or cash buyout of underwater options without shareholder approval
- The plan is a vehicle for problematic pay practices or a pay-for-performance disconnect
- The plan contains any other features that are determined to have a significant negative impact on shareholder interests, such features may include:
  - Tax gross-ups on equity awards
  - Provisions for reload options

[As we noted in our November Client Alert](#), EPSC factors fall into three categories: Plan Cost, Grant Practices, and Plan Features. Individual company scorecards and factor weightings have been developed for index groups based on a company’s membership in one of the following groups: S&P 500, Russell 3000 (excluding S&P 500), Non-Russell 3000 and IPO/Bankruptcy. IPO/Bankruptcy companies will not be subject to factors in the Grant Practices category for three fiscal years.

	Maximum Pillar Score		
	Plan Cost	Grant Practices	Plan Features
S&P 500 & Russell 3000	45	35	20
Non-Russell 3000	45	25	30
		<small>Burn Rate &amp; Duration only</small>	
IPO/Bankruptcy	60	---	40

ISS has not disclosed the weightings for individual factors, but we know EPSC factors are not equally weighted. ISS provided the following EPSC factors and basis for scoring in the recently released FAQs:

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Plan Cost	Definition	Scoring Basis
Shareholder Value Transfer (SVT)	<p>1. New shares requested <i>plus</i> shares remaining for future grants, <i>plus</i> outstanding unvested/unexercised grants.</p> <p>2. Only new shares requested <i>plus</i> shares remaining for future grants.</p>	Score is scaled based on company's SVT vs. ISS benchmarks. Maximum points given to proposals with total costs $\leq$ 65% of benchmark SVT.

Grant Practices	Definition	Scoring Basis
Three-year Average Burn Rate	Company's three-year average burn rate relative to industry and index peers. Industry based on GICS classification. Index classifications are S&P 500, Russell 3000 or Non-Russell 3000.	Score is scaled based on company's burn rate vs. ISS benchmarks (see appendix)
Estimated Plan Duration	Estimated time the proposed share reserve (including existing reserve) will last. Calculated based on company's three-year average burn rate.	<p>Duration</p> <p><math>\leq</math> 5 years = full points</p> <p><math>&gt;5 - \leq</math> 6 years = <math>\frac{1}{2}</math> of full points</p> <p><math>&gt;</math> 6 years = no points</p>
CEO's Equity Vesting Period	Period required for full vesting of the most recent equity awards received by CEO within the prior three years.	<p>Vesting Period</p> <p><math>&gt;</math> 4 years = full points</p> <p>3 - 4 years = <math>\frac{1}{2}</math> of full points</p> <p><math>&lt;</math> 3 years = no points</p>
CEO's Proportion of Performance-Conditioned Awards	Proportion of the CEO's most recent fiscal year equity awards (three-year look-back) that is conditioned on achievement of a disclosed goal.	<p>50% or more = full points</p> <p>33% <math>&lt;</math> 50% = <math>\frac{1}{2}</math> of full points</p> <p><math>&lt;</math> 33% = no points</p>
Clawback Policy	Does the company have a policy that would authorize recovery of gains from all or most equity awards in the event of certain financial restatements?	<p>Yes = full points</p> <p>No = no points</p>
Holding Period	Does the company require shares received from grants under the plan to be held for a specified period following their vesting/exercise?	<p><math>\geq</math>1 year or end of employment = full points</p> <p><math>&lt;</math> 1 year (or until ownership guideline met) = <math>\frac{1}{2}</math> full points</p> <p>No holding period = no points</p>

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Plan Features	Definition	Scoring Basis
CIC Single Trigger	Automatic vesting of outstanding equity awards upon a change in control.	Yes = no points No = full points
Liberal Share Recycling – Full Value Shares	Certain shares not issued (or tendered to the company) related to full value share vesting may be re-granted	Yes = no points No = full points
Liberal Share Recycling – Options/SARs	Certain shares not issued (or tendered to the company) related to option or SAR exercises or tax withholding obligations may be re-granted; or, only shares ultimately issued pursuant to SARs grants count against the plan's share reserve	Yes = no points No = full points
Minimum Vesting Requirement	Does the plan stipulate a minimum vesting period of at least one year for any award?	No or < 1 year = no points ≥ 1 year = full points
Full Discretion to Accelerate (non-CIC)	May the plan administrator accelerate vesting of an award (unrelated to a CIC, death or disability)?	Yes = no points No = full points

**OUR VIEW**

We believe that a well-designed and well-communicated equity plan is vital for all public companies and advise companies to seek timely shareholder input and support as part of the process in developing the equity plan proposal. It is crucial that companies develop a strategic shareholder outreach program that includes not only talking to major shareholders to highlight the objectives and rationale of the program, but listening to shareholders' feedback and potentially adjusting the plan design to reflect any concerns that are raised.

While ISS views can be an important consideration in long-term incentive plan design, these considerations should not trump the selection of design features which, when thoughtfully considered, result in a program aligned with the long-term strategic objectives of the organization and supportive of the responsible growth of shareholder value.

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With the adoption of the new EPSC approach, ISS has added additional flexibility, as well as complexity and nuance, to its equity plan evaluations. Plan cost, as measured by SVT benchmarks that are not disclosed, remains the most influential factor in determining ISS' voting recommendation. However, with the likelihood that most companies will not be able to maximize their score in the Plan Cost category, it is critical that companies review plan documents, three-year burn rates and historical CEO grant practices.

We are disappointed that ISS has not disclosed the weighting of individual factors. We continue to urge ISS to provide full transparency, similar to the levels they expect from companies. As companies consider whether or not to modify their plans to secure full credit under the EPSC, we believe they are entitled to understand the impact these changes will have on their score.

While ISS will now consider a range of factors under the EPSC, it is also our understanding that SVT and burn rate levels in excess of pre-determined (but undisclosed) thresholds will be deemed egregious practices which could be sufficient, in and of themselves, to trigger an "Against" recommendation.

We also note that due to the addition of the new S&P 500 category, 2015 burn rate benchmarks for most S&P 500 companies will be significantly lower than the applicable 2014 caps. This change will likely make it extremely difficult for many S&P 500 companies to receive the maximum points on the burn rate factor.

Please do not hesitate to contact your SH&P representative or Joseph Sorrentino to discuss further.

**ABOUT STEVEN HALL & PARTNERS**

Steven Hall & Partners is an independent executive compensation consulting firm, specializing exclusively in the areas of executive compensation, board remuneration, non-profit compensation and related governance issues. By focusing solely on this critical and complex segment of the human resources arena, we are able to provide our clients with the highest quality expertise and best counsel available on a practical basis. For more information, please visit [www.shallpartners.com](http://www.shallpartners.com) and follow us on Twitter [@SHallPartners](https://twitter.com/SHallPartners).

**CONTACTING STEVEN HALL & PARTNERS**

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**Contact**      Joseph Sorrentino      212-488-5400      [jsorrentino@shallpartners.com](mailto:jsorrentino@shallpartners.com)

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**ISS 2015 Burn Rate Benchmarks**

**S&P 500**

GICS	Description	Mean	Standard Deviation	Industry Benchmark
10	Energy	1.19%	0.56%	2.00%
15	Materials	1.25%	0.71%	2.00%
20	Industrials	1.44%	0.69%	2.13%
25	Consumer Discretionary	1.66%	0.84%	2.50%
30	Consumer Staples	1.42%	0.69%	2.11%
35	Health Care	1.99%	0.83%	2.82%
40	Financials	1.79%	1.46%	3.25%
45	Information Technology	3.24%	1.49%	4.73%
50	Telecommunication Services	0.95%	0.33%	2.00%
55	Utilities	0.82%	0.38%	2.00%

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**ISS 2015 Burn Rate Benchmarks**
**Russell 3000** (excluding S&P 500)

GICS	Description	Mean	Standard Deviation	Industry Benchmark
1010	Energy	2.55%	2.48%	5.03%
1510	Materials	1.60%	1.31%	2.91%
2010	Capital Goods	1.93%	1.22%	3.15%
2020	Commercial & Professional Services	2.86%	1.70%	4.56%
2030	Transportation	1.84%	2.07%	3.91%
2510	Automobiles & Components	2.02%	1.35%	3.37%
2520	Consumer Durables & Apparel	2.32%	1.57%	3.89%
2530	Consumer Services	2.58%	1.63%	4.21%
2540	Media	2.65%	2.52%	5.17%
2550	Retailing	2.65%	1.81%	4.46%
3010, 3020, 3030	Consumer Staples	1.73%	1.42%	3.15%
3510	Health Care Equipment & Services	3.28%	1.85%	5.13%
3520	Pharmaceuticals & Biotechnology	3.78%	2.21%	5.99%
4010	Banks	1.67%	1.67%	3.34%
4020	Diversified Financials	4.56%	4.43%	8.99%
4030	Insurance	2.04%	1.80%	3.84%
4040	Real Estate	1.40%	1.31%	2.71%
4510	Software & Services	4.97%	2.91%	7.88%
4520	Technology Hardware & Equipment	3.65%	2.20%	5.85%
4530	Semiconductor Equipment	4.75%	2.15%	6.90%
5010	Telecommunication Services	3.03%	1.51%	4.54%
5510	Utilities	0.84%	0.54%	2.00%

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**ISS 2015 Burn Rate Benchmarks**

**Non-Russell 3000**

GICS	Description	Mean	Standard Deviation	Industry Benchmark
1010	Energy	2.51%	3.72%	6.23%
1510	Materials	3.09%	3.89%	6.98%
2010	Capital Goods	3.54%	3.96%	7.50%
2020	Commercial & Professional Services	3.88%	3.64%	7.52%
2030	Transportation	1.73%	2.14%	3.87%
2510	Automobiles & Components	2.19%	2.02%	4.21%
2520	Consumer Durables & Apparel	2.83%	3.05%	5.88%
2530	Consumer Services	2.71%	3.00%	5.71%
2540	Media	2.70%	2.49%	5.19%
2550	Retailing	3.79%	2.72%	6.51%
3010, 3020, 3030	Consumer Staples	2.36%	2.96%	5.32%
3510	Health Care Equipment & Services	4.56%	3.91%	8.47%
3520	Pharmaceuticals & Biotechnology	4.86%	3.86%	8.72%
4010	Banks	1.20%	1.80%	3.00%
4020	Diversified Financials	2.28%	4.11%	6.39%
4030	Insurance	1.06%	1.68%	2.74%
4040	Real Estate	0.93%	1.44%	2.37%
4510	Software & Services	4.62%	3.70%	8.32%
4520	Technology Hardware & Equipment	4.07%	3.91%	7.98%
4530	Semiconductor Equipment	4.44%	4.26%	8.70%
5010	Telecommunication Services	3.67%	3.66%	7.33%
5510	Utilities	1.81%	2.21%	4.02%