2011 U.S. Postseason Report

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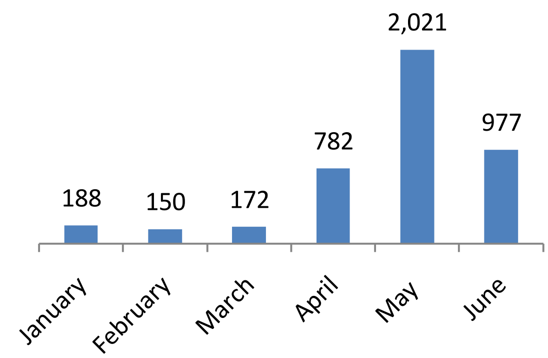
Number of U.S. Annual Meetings Covered by ISS During Proxy Season 2011



Key Takeaways

- During the first year of advisory votes on executive compensation under the Dodd-Frank Act, investors overwhelmingly endorsed companies' pay programs, providing 92.1 percent support on average. Through Sept. 1, shareholders voted down management "say on pay" proposals at 38 Russell 3000 companies, or just 1.6 percent of the total that reported vote results. Most of the failed votes apparently were driven by pay-for-performance concerns.
- “Say on pay” votes increased investors’ workloads, but spurred greater engagement by companies and prompted some firms to make late changes to their pay practices to win support.

- Investors overwhelmingly supported an annual frequency for future pay votes. As of Sept. 1, annual votes had garnered majority (or plurality) support at 80.1 percent of companies in the Russell 3000 index, as compared to triennial votes, which won the greatest support at 18.5 percent of issuers.
- The number of directors at Russell 3000 firms that failed to garner majority support fell by nearly half as say on pay votes presented shareholders with an alternative to votes against compensation committee members. Poor meeting attendance, the failure to put a poison pill to a shareholder vote, and the failure to implement majority-supported shareholder proposals were among the reasons that contributed to majority dissent against board members this year.
- Among governance proposals, the biggest story of this year was the greater support for shareholder proposals that seek board declassification. These resolutions averaged 73.5 percent support, up more than 12 percentage points from 2010, and won majority support at 22 out of 23 large-cap firms.
- Majority voting proposals averaged almost 60 percent support, while proponents reached settlements with more than 30 firms. Independent chair proposals fared better this year, winning majority support at four companies.
- There were fewer shareholder proposals to repeal supermajority rules, as more companies put management proposals on the ballot.
- Investor support for shareholder resolutions on environmental and social (E&S) issues continues to rise. This year, there was a 20.6 percent average approval rate for these proposals, the first time this support level had reached the 20 percent mark. Five proposals received a majority of votes cast, a new record.

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Management Say on Pay (MSOP)

The light of reform loomed large during the 2011 proxy season. When the first shareholder proposal seeking "say on pay" was filed in the U.S. in 2006, no one could have predicted how quickly these proposals would become common. In early 2009, there was an unexpected requirement that Troubled Asset Relief Program (TARP) companies include such proposals on their ballots. As required by the Dodd-Frank Act, these proposals appeared on the majority of U.S. proxy statements in 2011.

For 2011 and beyond, the Dodd-Frank Act has mandated an advisory vote on executive compensation for all U.S. companies, while companies with a market capitalization below $75 million are exempted from such requirement until 2013.

During this first year of nearly universal advisory votes on executive compensation under the Dodd-Frank Act, investors have overwhelmingly endorsed companies' pay programs, providing 92.1 percent support on average at Russell 3000 constituents as of Sept. 1 (based on "for" and "against" votes). Within the ISS coverage universe, the average support for companies' pay programs was 91.4 percent. This support exceeds the 89.2 percent average approval in 2010, when "say on pay" votes were mandated only at TARP firms. While the median total compensation for CEOs at S&P 500 firms increased by more than 33 percent last year, those pay increases haven't translated into more shareholder opposition, in part because of the underlying spirit of the "say on pay" mandate: greater engagement with investors by issuers. Notably, dozens of companies released supplemental proxy materials to address investor concerns or made late changes to their pay practices to win shareholder support, in most cases, after engaging with large shareholders. For example, subsequent to its proxy filing, General Electric filed additional proxy materials disclosing that, as a result of discussions with certain shareholders, the company agreed to attach performance conditions to stock options awarded to CEO Jeffrey Immelt.

Support varied slightly across sectors: the lowest average approval was observed in the energy sector at 89.1 percent, while the financial services and consumer retail sectors tied for the highest average level of support at 92 percent.

Figure 1: Average Support for MSOP by Sector (As of Sept. 1)

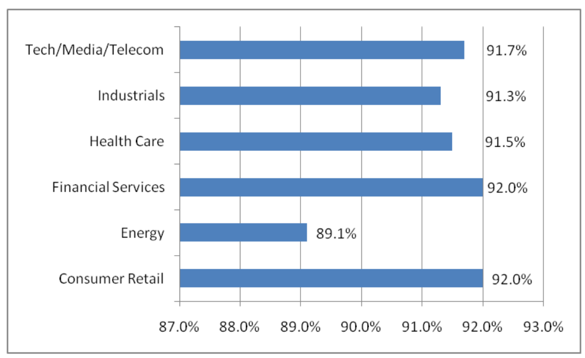
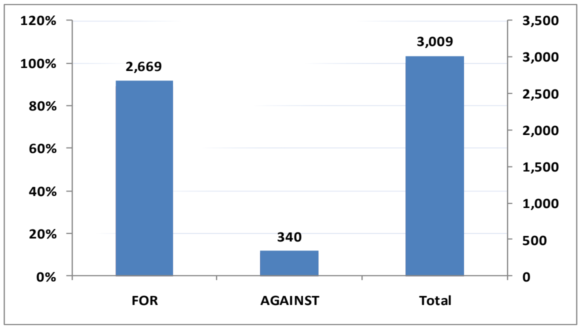


Figure 2: MSOP – ISS' Vote Recommendations



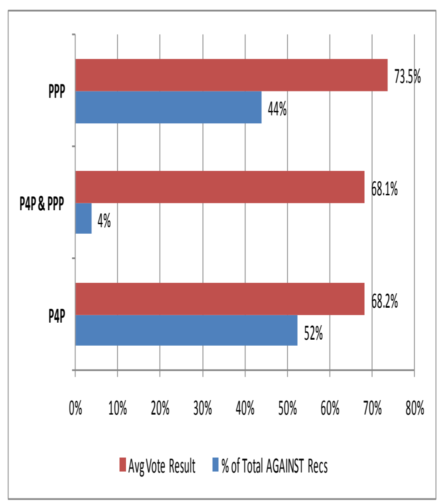
As of Sept. 1, ISS had issued recommendations on about 3,009 management "say on pay" proposals, supporting 2,669, or approximately 88.7 percent of all proposals. ISS recommended in favor of approximately 85 percent of MSOPs at S&P 500 companies, 88 percent at Russell 3000 companies (exclusive of S&P 500 issuers), and 93 percent at non-Russell 3000 companies. Where ISS recommended voting against "say on pay" proposals at S&P 500 firms, average support by shareholders was 65 percent, compared with the overall large-cap average support of 89 percent.

The financial services sector accounted for the highest number of MSOPs with a quarter of the total. Meanwhile, the energy sector witnessed the highest MSOP opposition rate from ISS (15 percent) followed closely by the consumer retail sector (14 percent).

Reasons for ISS Opposition

As of Sept 1, ISS had recommended that shareholders vote against 340 MSOPs, or about 11 percent of such proposals analyzed as of that date. For the most part, ISS opposed MSOPs due to pay-for-performance misalignment (P4P), which represented over half (52 percent) of all against recommendations, followed by concerns around problematic pay practices (PPPs) that accounted for 44 percent of all against recommendations. Four percent of ISS' recommendations resulted from concerns around the presence of *both* P4P disconnects as well as PPPs. Seventy-two percent of the P4P inspired negative recommendations were issued at Russell 3000 firms, while almost a quarter of the P4P recommendations were issued at S&P 500 firms. Sixty-nine percent of ISS' negative recommendations due to PPP concerns occurred at Russell 3000 firms, 17 percent at considerably smaller issuers outside the Russell 3000, and the remaining 13 percent were at S&P 500 firms. Shareholder support levels were lowest where both P4P and PPP concerns were present as well as where P4P concerns were raised.

Figure 3: Reasons for ISS Recommendations Against MSOP and Average Support Levels



On a sector basis, a pay-for-performance disconnect was most prevalent in the financial services sector, followed closely by the industrials and technology/media/telecom (TMT) sectors. The financial services sector again drew most of the negative recommendations, which were driven by PPP concerns followed by the consumer retail and TMT sectors, tied in second place. Investor support levels were lowest in sectors where both P4P and PPP concerns were identified. P4P concerns resulted in the lowest shareholder support levels at firms in the energy sector, and vote tallies were lowest in the industrials sector where PPP concerns were raised.

On a combined sector and indices basis, S&P 500 firms in the financial services sector witnessed the highest level of opposition from ISS for pay-for-performance disconnects. In the Russell 3000 universe, the sectors with the highest number of pay-for-performance disconnects were the financial services and TMT sectors, which saw identical degrees of opposition from ISS on their pay programs.

Figure 4: ISS Recommendations Against MSOP Based on P4P Disconnects by Sector

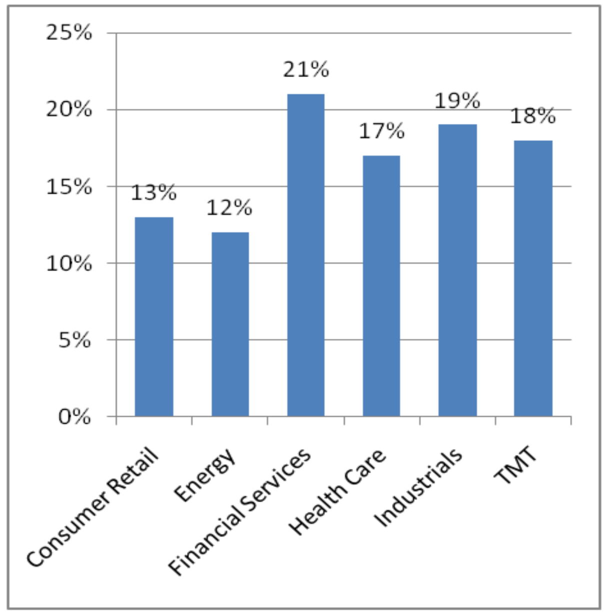


Figure 5: ISS Recommendations Against MSOP based on PPP by Sector

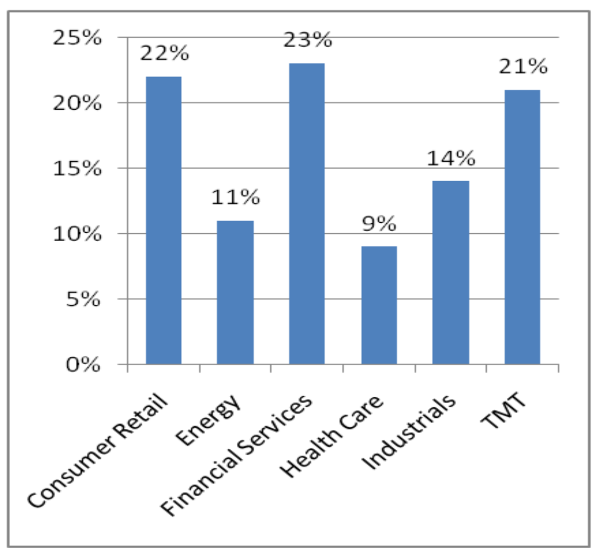
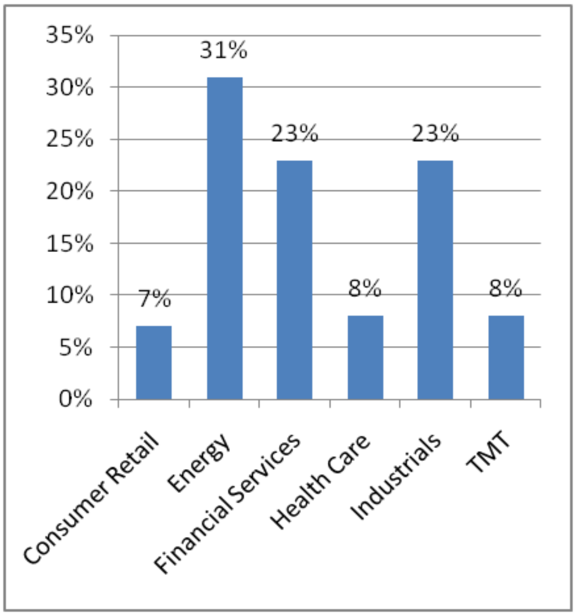


Figure 6: ISS Recommendations Against MSOP Based on both P4P & PPP by Sector



Failed Votes

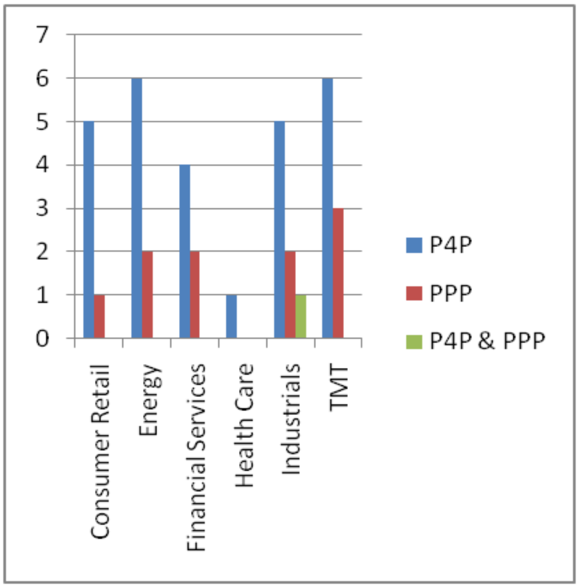
To date, shareholders have voted down management "say on pay" proposals at 38 U.S.-listed companies in the Russell 3000 index, or approximately 1.6 percent of the more than 2,200 companies in the index for which vote results were available. This list includes three companies (Weatherford International Ltd., Cutera, and Dex One) that have since left the Russell 3000 index. This list doesn't include three issuers (Hemispherx BioPharma, Cooper Industries, and Doral Financial) where the advisory votes would have failed if abstentions had been included in the calculation. Companies generally employed a majority of votes cast vote standard on their MSOP agenda items, where abstentions were not counted.

Of the 38 companies with failed votes as of Sept. 1, 11 received less than 40 percent support of the votes cast "for" and "against." Overall, eight S&P 500 companies and 30 Russell 3000 firms have failed to receive majority support for their executive pay programs.

The primary driver of these failed votes appears to be pay-for-performance concerns, which were identified at 28 companies. Investors appear to have voted their pocketbooks this proxy season. Almost half of the failed-vote firms have reported double-digit negative three-year total shareholder returns. Also contributing to investor dissent were issues like tax gross-ups, discretionary bonuses, inappropriate peer benchmarking, excessive pay, and failure to address significant opposition to compensation committee members in the past.

The greatest number of failed advisory votes with pay-for-performance as the underlying issue--about 22 percent--occurred in the energy sector, where companies such as Helix Energy Solutions, Superior Energy Services, and Constellation Energy received some of the lowest levels of shareholder support. At Constellation, shareholder support was only 38.6 percent, which appears to be due to pay-for-performance concerns at the company. CEO Mayo Shattuck's total compensation increased from $6.7 million in 2009 to almost $16 million in 2010. Meanwhile, the company's one- and three-year total shareholder returns were negative 10.3 percent and negative 30.6 percent, respectively. Shattuck's total pay increase was primarily due to a significant increase in his deferred compensation and pension value, and in the value of stock options granted to him. However, although his annual cash bonus declined by $1.3 million (to $1.7 million), he also received an award of time-based restricted shares valued at $1.5 million in 2010, compared with none the prior year.

Figure 7: Failed MSOP Proposals & Reasons by Sector (38 Companies as of Sept. 1)



Shareholders also expressed significant opposition at homebuilders NVR, Beazer Homes USA, and M.D.C. Holdings, and there was majority dissent at several real estate development firms, such as BioMed Realty Trust and Kilroy Realty.

Other well-known companies with failed "say on pay" votes this year include: Stanley Black & Decker (which reported large time-based and guaranteed equity awards, and failed to address low voting sup-port for two compensation committee members in 2010); Nabors Industries (where ISS identified pay-for-performance concerns, coupled with pay significantly above the peer group median); Hewlett-Packard (where ISS raised concerns over the new CEO's hire package in conjunction with a track record of generous severance payments for departing executives, and the CEO's participation in selecting new board members who will oversee his pay); Janus Capital Group (which reported a large sign-on bonus for the new CEO, despite lagging shareholder returns); Jacobs Engineering Group (where ISS identified pay-for-performance concerns), and Masco (also pay-for-performance). The lowest support was garnered at Cincinnati Bell's annual meeting in May, where the proposal failed with the support of 29.8 percent of votes cast.

In addition to the failed votes, more than 41 companies received between 50 and 60 percent support for their pay practices, and may face greater shareholder scrutiny next year. Among those firms were Chesapeake Energy, Safeway, Lazard, Amgen, Devon Energy, and Allstate.

Voting Mechanics

At three companies, Hemispherx BioPharma, Cooper Industries, and Doral Financial Corp., the role of abstentions in determining the outcome has been a challenge for investors. In addition, Toreador Resources stated in a filing that the MSOP resolution was approved with the following vote results:

For	Against	Abstain	Broker Non-votes
8,240,534	600,311	8,250,534	10,538,673

This is an unusual case, where the "for" votes far exceed the "against" votes, but the "for" total is identical to the abstention total, which is statistically improbable and may suggest a reporting error by the company. Also, the total 27.5 million votes (including broker votes) on the MSOP agenda item far exceed all the votes on the other agenda items, which are around 19 to 20 million.

At Hemispherx, the "for" votes exceeded the "against" votes but there were a significant (almost 16 percent) number of abstentions. After the vote, the company reported that shareholders "approved" its executive compensation.

The resolution at Doral Financial was approved, according to the company, even though the proposal received support of less than a majority of the votes cast at the meeting when abstentions were counted (For: 39,4245,812; Against: 23,288,725; Abstain: 17,393,908; Broker Non-Votes: 27,477,064). Based on the company's required vote for this resolution, abstentions were not taken into account for calculating the level of support for the proposal. At Cooper Industries, the situation is similar to that at Doral Financial, where the resolution passed according to the company's vote standard, which excluded abstentions.

Pay-for-Performance Disconnects: In the Eye of the Beholder?

ISS Pay-for-Performance Evaluations

Shareholders and institutional investors continue to consider pay for performance an integral aspect of executive compensation. During the first year of the MSOP mandate, pay for performance has again proven to be pivotal to proxy voting decisions by institutional investors. Since 2004, the ISS pay-for-performance policy has played a central role in evaluating the CEO compensation of Russell 3000 companies in context of financial performance. In the face of new disclosure obligations, legislation over pay practices, and the advent of "say on pay," ISS has continued to streamline its policies, and integrated the pay-for-performance analysis into an executive compensation evaluation policy (ECEP), along with other longstanding policies such as those on problematic pay practices, equity compensation, and "say on pay."

Since 2009, when ISS first shifted to a relative TSR standard of measurement against the median of GICS peers, approximately one-third of the Russell 3000 companies have had one-year and three-year TSRs below their peer group median, and this continues to be the case for 2011.

The ISS case-by-case pay-for-performance analysis was also expanded before the 2010 proxy season to take into consideration a longer horizon in evaluating the alignment of company performance and CEO pay. The current policy approach remains in place when identifying potential disconnects in cases where the company's total shareholder return (TSR) is below the median of comparable peers (within the company's four-digit GICS group), and the year-over-year change in the CEO's total compensation does not appear to be aligned with that underperformance. Factors considered include the nature of the pay increase (i.e., whether it is appropriately performance based) and the CEO's total pay relative to the median of a peer group based on companies of similar size and industry group. The additional evaluative factor added in 2010 considers the alignment of trends in the CEO's pay changes and the company's TSR over the prior five years. This approach allows shareholders a longer term view as well as an absolute view of pay and performance alignment.

As it continues to evolve, ISS' pay-for-performance analysis seeks to give shareholders a better view of the efficacy of increasingly complex executive compensation programs. According to the ISS 2009-2010 policy survey, 94 percent of institutional investor respondents believed that pay-for-performance plays either a “critical” or “important” role in evaluating executive compensation.

As of Sept. 1, out of approximately 2,300 annual and special meetings at Russell 3000 constituents, ISS has identified 811 or 35 percent of that universe as relative underperformers. ISS defines underperformance as last 1- and 3-year total shareholder returns (TSRs) below the median TSR of a company's 4-digit GICS group within the Russell 3000 index. Notably, out of the 811 underperformers in the Russell 3000 Index, ISS has identified 183 pay-for-performance disconnects – or approximately 22.5 percent of the underperforming universe of companies in the Russell 3000 Index. Only 27 of the management sponsored say-on-pay proposals at these companies failed to garner majority shareholder support. Notably, however, the 27 failed resolutions make up the lion's share, 73 percent, of failed say-on-pay resolutions during the proxy season under review.

Figure 8: Pay for Performance per ISS Policy

	2008	2009	2010	2011*
Underperforming companies	487	975	925	811
Pay-for-Performance Disconnect: number of companies	43	69	100	183
Pay-for-Performance Disconnect: percentage of underperformers	8.8%	7.0%	11.0%	22.5%

*As of Sept. 1

CEOs at 319 companies out of the 811 underperforming Russell 3000 Index constituents saw an increase in year-over-year total compensation, while 492 CEOs saw a decline in their total compensation. Average CEO tenure at these 811 companies was 7.4 years, with a median of 5.5 years of tenure in the CEO post. While the number of underperforming companies changed little from 2010 (925) to YTD 2011 (811), the number of companies that ISS identified with pay-for-performance misalignment more than doubled during the same period. This could be due, in part, to companies seeking to "make-up" forgone compensation in the preceding years in light of the economic downturn. Such additional compensation in fiscal 2010, at the P4P disconnect companies, was delivered mostly in the form of non-performance-based pay, which remains to be the primary driver behind pay-for-performance disconnects. Despite the fact that only 6 out of the 183 companies, or about 3.3 percent, maintained guaranteed bonuses for their CEOs pursuant their employment agreements, discretionary cash and equity bonus payments in tandem with sustained relative underperformance was the most prevalent reason underlying a pay-for-performance disconnect.

Problematic Pay Practices: The Constant is Change in Change-in-Control Practices

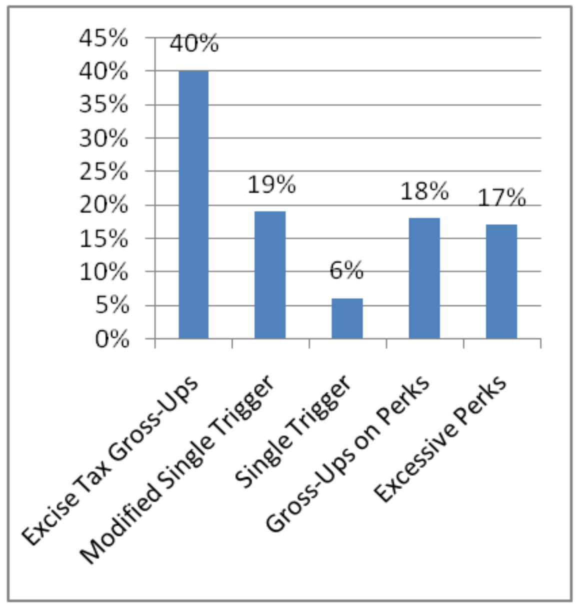
Many companies announced new pay reforms in their 2011 proxy statements. The most common changes, by far, continue to be related to change-in-control practices, and more specifically to excise tax gross-ups. Excise taxes are only due in connection with certain excessive payments related to a change of control, i.e., when an executive's payout exceeds a defined threshold. The original intention of Congress, when it defined an "excess" parachute, was to limit the size of such packages by creating tax disadvantages for both the company and the individual in such cases. One unintended consequence of that legislation was a move by many companies to insulate the executive from his or her potential adverse tax consequences. That trend has been changing, however, as shareholders have begun to question the appropriateness and need for such gross-ups.

Companies eliminating excise tax gross-ups, in either current or future agreements, cite evolving best practices, feedback from shareholders, the advice of consultants, and a report from the Conference Board as well as the changing policy of proxy advisory organizations (ISS has deemed such gross-ups a problematic practice since 2008). Or, some companies even eliminated the practice without a stated rationale. On March 18, 2011, the Walt Disney Co. sent the following communication to certain shareholders: "We would like to make you aware that we have amended employment agreements with four executives to remove a provision that provided for gross-ups for excise tax payments the executives could incur upon termination following a change in control."

As previously mentioned, a majority of ISS' recommendations against say-on-pay proposals were based on pay-for-performance disconnects; however, investors should note that the lowest rate of support on average was garnered at companies which exhibited problematic pay practices in tandem with a pay-for-performance disconnect.

While approximately 44 percent of companies received an adverse vote recommendation from ISS solely based on problematic pay practices, 13 companies had also exhibited a pay-for-performance disconnect in tandem with employing problematic pay practices – out of the total 340 companies that received adverse vote recommendations from ISS on their MSOPs. While the most prevalent problematic pay practice observed during this proxy season continued to be excise tax gross-ups pursuant to new and/or extended employment/severance agreements with executives, many companies (more than 300 Russell 3000 constituents as of Sept. 1) have taken steps to eliminate the practice.

Figure 9: Problematic Pay Practices



*In new or materially amended employment/severance agreements

Impact of 'Say on Pay': More Engagement

While some activist investors and news organizations were disappointed by the low number of failed votes this year, others claim that the Dodd-Frank-mandated advisory votes had a positive impact by encouraging greater engagement and prodding firms to improve their pay practices.

These provisions are forcing many companies to reconsider their executive pay policies and ratchet back some of the most abusive practices, such as tax gross-ups and lavish severance packages," said Ann Yerger, executive director of the Council of Institutional Investors.

Several notable companies made late changes to their compensation programs or filed additional proxy materials to win shareholder support, including Walt Disney Co., General Electric, Alcoa, Collective Brands, and Assured Guaranty Ltd. At least 50 issuers have made additional filings to address investor concerns and proxy advisers' recommendations. In most cases, the companies objected to the industry peer groups and option-valuation methods used by the proxy advisers.

In a June 10 speech to the Social Investment Forum, SEC Commissioner Luis Aguilar observed that advisory votes appear to be facilitating an increase in communication between issuers and shareholders, and have resulted in positive changes to many companies' executive pay practices.

"Many companies are putting in more performance-based compensation plans and they are addressing items that shareholders often criticized, such as: excessive severance; perks; federal income tax payments; and pensions. For example, approximately 40 of the Fortune 100 companies have eliminated policies that had the company pay certain tax liabilities of executives," said Aguilar, who also mentioned the positive changes by General Electric.

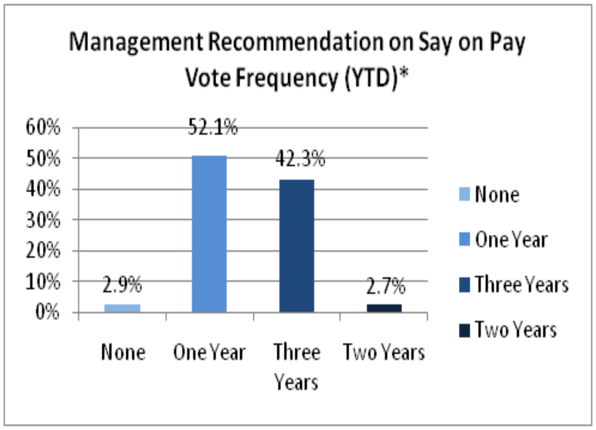
"There seems to be real evidence that "say on pay" is one catalyst to increasing shareholder engagement more broadly," Aguilar said.

According to the ISS 2011-2012 policy survey, 57 percent of institutional investor respondents stated that they had "more engagement with issuers in 2011."

'Say on Pay' Frequency Vote – Say When on Pay

The Dodd-Frank Act, in addition to requiring advisory votes on pay (MSOP), requires that the proxy for the first annual or other meeting of the shareholders occurring after the enactment include an additional advisory vote to determine whether the frequency of future MSOP votes will occur every one, two, or three years. A new vote regarding the frequency of the compensation approval vote must be taken by shareholders not less often than once every six years. Figures 10 and 11 summarize the voting trends for this type of proposal as of Sept. 1.

Figure 10:

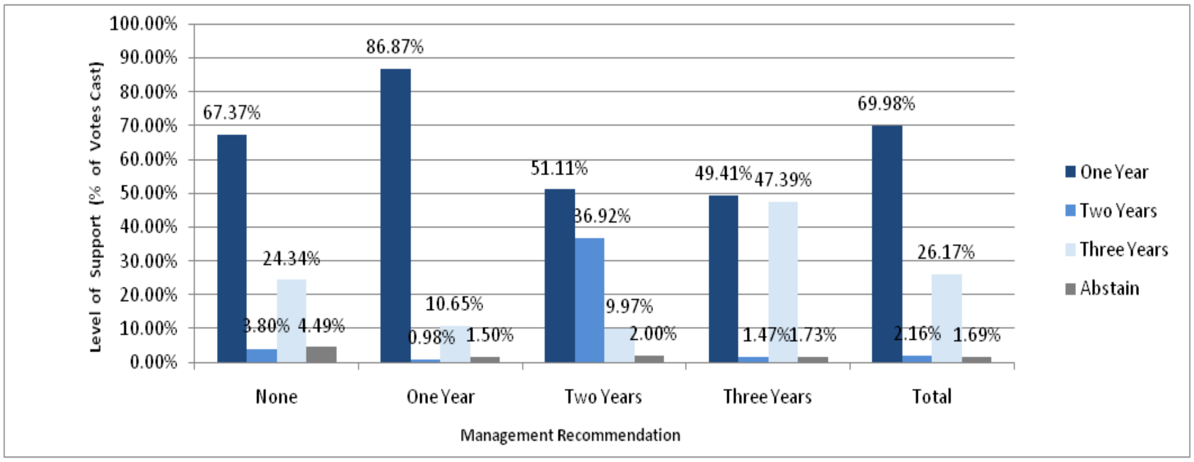


*Jan. 1 to Sept. 1, 2011

Notably, management recommendations on pay vote frequency shifted throughout proxy season. In the early part of proxy season, from March to mid-April, management recommendations shifted away from triennial votes and toward annual votes, following early investor support for an annual frequency. Overall, 51.6 percent of companies in the Russell 3000 Index with Sept. 1 or earlier meeting dates recommended for annual votes, while 43.6 percent endorsed triennial votes. Recommendations for biennial votes decreased throughout proxy season, stabilizing at around 2.3 percent. Another 2.3 percent of companies made no recommendation.

Management preferences did not appear to have a significant influence on the outcome of these frequency votes, as shown below. As of Sept. 1, investors had defied management recommendations for triennial votes at 538 of 892 Russell 3000 companies, according to ISS data. Shareholders also were not swayed by biennial recommendations at 34 out of 47 issuers in the Russell 3000 Index. The annual vote option garnered, on average, somewhat higher rate of support than the triennial option even when managements recommended the triennial option, and shareholders showed a clear preference for annual pay votes when management made no frequency recommendation.

Figure 11: Shareholder Votes on MSOP Frequency by Management Recommendation



While most U.S. companies have indicated that they would heed shareholders' views on the frequency of future "say on pay" votes, there are a few exceptions. Annaly Capital Management and American Reprographics both have said they will hold triennial votes, even though investors gave majority support for annual votes. Voting results show that shareholders have overwhelmingly supported an annual frequency. As of Sept. 1, annual votes have garnered majority support at 958 companies in the Russell 3000 index, as compared to 354 triennial votes, and just 13 biennial votes.

Frequency Vote Outcomes by Voting Option and Management Recommendation

Figure 12: MSOP Frequency Votes: Majority Support by Management Recommendation

	Management Recommendation				
Vote Results (majority of votes cast)	**None**	**1 Year**	**2 Year**	**3 Year**	**Total**
1 Year	83.9%	99.5%	60.3%	53.7%	78.9%
2 Year	1.6%	0%	24.1%	0%	0.7%
3 Year	11.3%	0.4%	0.0%	39.5%	17.1%
Abstain	0.0%	0.1%	0.0%	0.1%	0.1%
No option received majority support	3.2%	0.0%	15.5%	6.7%	3.4%

Figure 13: MSOP Frequency Votes: Number of Proposals

	Management Recommendation				
Vote Results (majority of votes cast)	**None**	**1 Year**	**2 Year**	**3 Year**	**Total**
1 Year	52	1186	35	507	1780
2 Year	1	0	14	0	15
3 Year	7	5*	0	373	385
Abstain	0	1*	0	1	2
no option received majority support	2	0	9	63	76
Total	**62**	**1192**	**58**	**944**	**2256**

*Resolutions where management recommended an annual vote, where the voting outcome was different than the management recommendation. At Monarch Casino & Resort Inc., Trident Microsystems Inc., Schweitzer-Mauduit International Inc., ManTech International Corp., and Digital River Inc., the triennial frequency received majority support. At Amkor Technology, management recommended an annual frequency, but a management-affiliated trust (with a 44.6 percent stake) abstained.

Golden Parachute Votes

The Dodd-Frank Act also requires companies to hold separate shareholder votes on "golden parachute" arrangements when they seek approval for mergers, sales, and other transactions. However, the SEC rules on this mandate did not take effect until April 25, so few companies held parachute votes during proxy season.

As of Sept. 1, only 14 Russell 3000 companies had conducted golden parachute votes, and only six received more than 89 percent support. At SAVVIS Inc., where the sale of the company to CenturyLink earned nearly unanimous investor approval, the severance arrangements only garnered 69 percent shareholder support. It appears that investors had concerns over $3.9 million in potential (excise) tax gross-up payments for CEO James Ousley. However, the other vote results suggest that investors will tend to support a company's golden parachute payments if they believe that the overall transaction has merit. Nevertheless, the average shareholder support at these 14 companies was approximately 86 percent, which is significantly lower when compared to the average support level for the underlying transactions combined, which was over 90 percent. While still early, these results suggest that many investors do view the golden parachute proposal separately from the underlying change-in-control transaction, meaning that they might still oppose the golden parachute payments while supporting an underlying transaction.

Given the low number of golden parachute votes to date, it may be too early to draw significant conclusions regarding their impact on future pay practices. Such votes may present opportunities for shareholders to continue pressuring firms to curb problematic change-in-control arrangements with executives.

Management Equity Proposals

From the beginning of the year through Sept. 1, 2011, approximately 1,136 equity incentive plans were submitted to shareholders, excluding broader-based plans such as employee stock purchase plans (ESPP). By comparison, for similar periods in 2010, 2009, and 2008, ISS evaluated 1,167, 1,160, and 1,300 plans, respectively. Approximately 63 percent of the proposals pertained to the amendment of existing compensation plans, while the remaining 37 percent sought to establish new plans.

More than half of the plan amendments sought to authorize additional share issuances under prior plans. Specifically, this consisted of 647 of the proposals from the total 716 plan amendments brought to shareholder vote. Although other plan amendments may be more administrative in nature, such as the usual re-approval for Section 162(m) compliance purposes, some others sought the extension of plan life or plan participants or, more frequently, sought the inclusion of new forms of awards to be granted under the plan, especially restricted stock or units. This trend coincides with more companies actively considering incorporating full share or share-based awards into their programs, deemed to be more effective in terms of cost and retention strategy, compared to a heavier emphasis on options in prior years.

Figure 14: Equity Plan Proposals Voting Summary

Plan Amendment Proposals	For	Against	Totals
2011	490	226	716
2010	493	262	755
2009	536	248	784
New Plan Proposals			
2011	292	128	420
2010	254	158	412
2009	231	145	376

Equity Plan Proposals

Similar to past years, the predominant reason for ISS recommendations against equity plans remains high cost, in terms of shareholder value transfer (SVT) (relative to other companies in the same sector, taking into account size and performance). For instance, of the 354 negative recommendations issued by ISS on equity plan resolutions from January to September of this year, 266 demonstrated high SVT cost, or approximately 75 percent. It is important to note that, in these cases, there may be contemporaneous problematic features also identified. For example, 21 percent (57) of the compensation plans with high SVT costs were also found to explicitly allow for option repricing without prior shareholder consent. Notably, however, 48 plans received adverse vote recommendations from ISS based solely on explicitly allowing for option repricing without prior shareholder consent, or

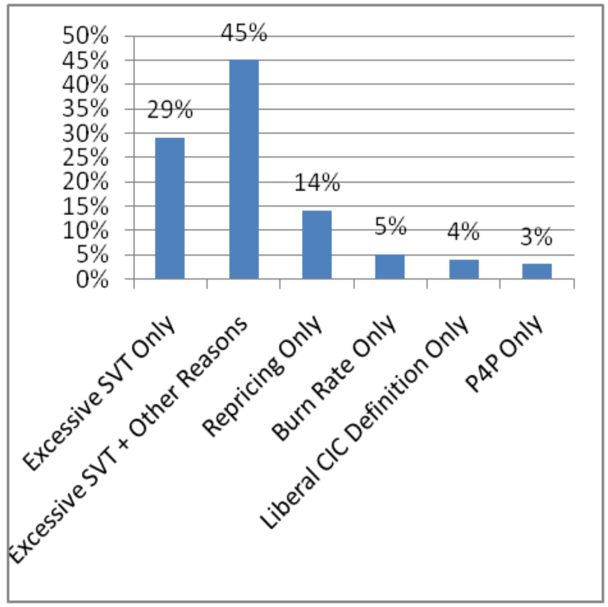
18 percent of the total (354) against recommendations rendered year to date.

Another problematic factor affecting equity plan proposals was excessive average burn rates (grant rates), which was found in 99 cases.

In all but 17 cases, the high burn rate also was coupled with high SVT cost. There were 34 cases where liberally defined change-in-control definitions were considered problematic (due to a combination with single-triggered vested acceleration upon a change in control), but the change-in-control trigger was considered to be the sole reason for not supporting the plan in only 15 of those cases. In a small percentage of cases, pay-for-performance disconnects driven by equity awards led to a negative recommendation on an equity plan proposal.

High SVT cost relative to a company's peers continues to account for most of the recommendations against equity plan proposals. The proposals that had a reasonable SVT cost but received a negative recommendation based on another reason comprised only 22 percent of the entire "adversely recommended" cases, whereas 75 percent of the adverse recommendation cases exhibited excessive SVT costs.

Figure 15: Reasons Underlying Adverse ISS Vote Recommendations



Failed Plans

Of the 354 negative recommendations issued by ISS on equity plan resolutions from January to September of this year, only four plans failed to garner majority support from shareholders, in addition to one at IRIS International Inc., where ISS had issued a FOR recommendation.

ISS observed more companies with proposed plans exhibiting high cost and excessive burn-rate at smaller cap companies during the proxy season under review. Specifically, while ISS recommended against on 5 percent of proposed plans at S&P 500 constituents, the level was much higher at the Russell 3000 (25 percent of plans), and even higher at non-Russell 3000 companies (56 percent of all plans). The vote results, however, paint a different picture. The level of shareholder support for plans at S&P

500 companies where ISS had a negative vote recommendation was considerably lower than it was at Russell 3000 Index companies, as well as at smaller cap companies. Plans at non-Russell 3000 companies that exhibited high potential costs to shareholder from an ISS perspective garnered, on average, 83 percent shareholder support, compared with 68.5 percent at S&P 500 companies.

The highest percentage of proposals came from the TMT sector (23 percent), followed by the industrials and health care sectors (19 percent and 18 percent of all plans, respectively). However, the financial services sector accounted for the highest percentage of the negative recommendations issued by ISS (37 percent), followed by the health care (33 percent) and consumer retail (32 percent) sectors, respectively. Interestingly, shareholder opposition was highest in the TMT sector, where the overall average support was 80.4 percent of votes cast, compared to, for example, 85 percent in the health care sector.

Combining the sector and index views reveals that amongst large cap firms, the TMT sector had the largest number of plans voted on (22 percent) and an ISS opposition rate of 6 percent, followed closely by the consumer retail sector, which represented 19 percent of all plans. S&P 500 firms in the financial services sector drew the highest opposition from ISS, a 16 percent opposition rate.

Fewer Shareholder-Sponsored, Compensation-Related Proposals

There were far fewer compensation-related investor proposals this season, primarily because of the absence of shareholder “say on pay” proposals. During the spring proxy season, just 32 compensation-related resolutions went to a vote, down from 86 during the first half of 2010. With the arrival of market-wide advisory votes, proponents focused on secondary compensation issues this year, such as the vesting of stock options and performance-based stock.

Proposals seeking shareholder approval of future golden parachute payments averaged 45 percent support at four companies and won majority approval at Lowe’s Companies and Whirlpool. While the Dodd-Frank Act allows companies to include severance benefits in their “say on pay” votes, the SEC ruled--in a no-action challenge by Navistar--that the law doesn’t preclude proposals that seek investor approval of future arrangements.

Also winning broad support this season were the Amalgamated Bank’s proposals that seek to prohibit the accelerated vesting of stock options. Those proposals averaged 41.5 percent approval and received 45.2 percent at Sunoco. Resolutions seeking performance-based stock earned almost 35 percent support at four companies; the best showing was 42.6 percent approval at Walgreen.

Retail investor Gerald Armstrong filed a new proposal this year that seeks a shareholder vote on director pay, which is not covered by the Dodd-Frank Act’s votes on executive pay. This proposal had single-digit support at three companies, but won an impressive 46.4 percent approval at Chesapeake Energy, where directors receive the rare perk of personal usage of the company aircraft.

At Bank of America's meeting, investors gave 35 percent support to a new shareholder proposal that seeks to ban reimbursement for relocating executives who lose money on the sale of their homes.

A new shareholder proposal that seeks to link executive pay to sustainability metrics did not fare well this year, averaging 5 percent support at four companies.

A Look Ahead to 2012

As investors prepare for a second year of market-wide advisory votes, many of them will be looking to see how companies respond to failed votes and significant dissent. While investors will have different thresholds for which firms they will scrutinize more closely, it appears likely that issuers with greater than 30 percent opposition this year will receive greater attention in 2012. During ISS' 2011-12 Policy Survey, 72 percent of investor respondents indicated on a cumulative basis that they expect to see an explicit board response at companies where dissent exceeded 30 percent. According to ISS data, 164 companies, or about 6 percent of the total, received more than 30 percent opposition this proxy season.

Shareholders will be looking to see if these companies make meaningful changes to address the linkage between pay and performance and other compensation concerns. If improvements are significant, investors likely will respond favorably. Two companies that suffered failed advisory votes in 2010--Occidental Petroleum and KeyCorp--made substantive changes to their pay practices and earned 91.3 and 86.7 percent support, respectively, this year. Occidental, for example, cut the CEO's long-term incentive opportunities by 70 percent, expanded the peer group used to benchmark pay, and reduced award opportunities for other named executives.

So far, at least two companies with failed 2011 votes have acted to address investor concerns. Helix Energy Solutions has said it would add performance metrics to its 2011 cash bonus program, while Umpqua Holdings has added performance conditions to previously awarded restricted stock and stock options.

If other companies don't adequately respond to this year's "say on pay" votes, investors may ramp up their protests and withhold support from more compensation committee members in 2012 and vote no during the advisory vote.

At the least, companies are required, pursuant to the Dodd-Frank Act, to include a discussion, in their proxy statement's compensation discussion and analysis section, about the vote results of the previous "say on pay" resolution and its implications on the company's compensation practices. Investors will simply be looking for more than just boiler-plate language in these discussions in evaluating the responsiveness of boards to vocalized shareholder concerns.

Figure 16. Failed MSOP Proposals in the Russell 3000 Index – as of Sept. 20

Company Name	Ticker	Meeting Date	Support (Includes Abstentions)	Result
Ameron International Corp.	AMN	3/30/2011	41.28%	Fail
Beazer Homes USA Inc.	BZH	2/2/2011	45.90%	Fail
BioMed Realty Trust Inc.	BMR	5/25/2011	45.75%	Fail
Blackbaud Inc.	BLKB	6/22/2011	44.67%	Fail
Cadiz Inc.	CDZI	6/2/2011	37.52%	Fail
Cincinnati Bell Inc.	CBB	5/3/2011	29.78%	Fail
Cogent Communications Group Inc.	CCOI	4/27/2011	39.27%	Fail
Constellation Energy Group Inc.	CEG	5/27/2011	38.04%	Fail
Curtiss-Wright Corp.	CW	5/6/2011	36.96%	Fail
Cutera Inc.	CUTR	6/14/2011	35.25%	Fail
Dex One Corp.	DEXO	5/3/2011	47.98%	Fail
Exar Corporation	EXAR	8/31/2011	49.10%	Fail
Freeport-McMoRan Copper & Gold Inc.	FCX	6/15/2011	45.46%	Fail
Helix Energy Solutions Group Inc.	HLX	5/11/2011	31.98%	Fail
Hercules Offshore Inc.	HERO	5/10/2011	38.44%	Fail
Hewlett-Packard Co.	HPQ	3/23/2011	48.25%	Fail
Intersil Corp.	ISIL	5/4/2011	44.18%	Fail
Jacobs Engineering Group Inc.	JEC	1/27/2011	44.82%	Fail
Janus Capital Group Inc.	JNS	4/28/2011	40.12%	Fail
Kilroy Realty Corp.	KRC	5/24/2011	48.51%	Fail
M.D.C. Holdings Inc.	MDC	4/27/2011	33.46%	Fail
Masco Corp.	MAS	5/10/2011	44.61%	Fail
Monolithic Power Systems Inc.	MPWR	6/16/2011	36.24%	Fail
Navigant Consulting Inc.	NCI	4/25/2011	44.80%	Fail
Nutrisystem Inc.	NTRI	5/12/2011	41.10%	Fail
NVR Inc.	NVR	5/3/2011	43.86%	Fail
Penn Virginia Corp.	PVA	5/4/2011	38.93%	Fail
PICO Holdings Inc.	PICO	5/13/2011	38.85%	Fail
Premiere Global Services Inc.	PGI	6/15/2011	47.32%	Fail
Shuffle Master Inc.	SHFL	3/17/2011	44.49%	Fail

Stanley Black & Decker Inc.	SWK	4/19/2011	37.95%	Fail
Stewart Information Services Corp.	STC	4/29/2011	47.83%	Fail
Superior Energy Services Inc.	SPN	5/20/2011	39.18%	Fail
The Talbots Inc.	TLB	5/19/2011	46.01%	Fail
Tutor Perini Corp.	TPC	6/1/2011	49.05%	Fail
Nabors Industries	NBR	6/7/2011	42.60%	Fail
Umpqua Holdings Corporation	UMPQ	4/19/2011	36.16%	Fail
Weatherford International Ltd.	WFT	5/25/2011	43.95%	Fail

Fewer Governance Proposals Filed This Proxy Season

The overall volume of governance proposals was down this season again and hit a new post-Enron low. For meetings held from Jan. 1 to Sept. 1, investors filed 488 governance proposals, down from 663 during the same period in 2010.

The primary reason for this drop was the absence of shareholder "say on pay" proposals, which accounted for 77 filings in 2010, and became unnecessary after the passage of the Dodd-Frank Act. The greater workload associated with marketwide advisory votes may have deterred some activists from filing more proposals.

Of the governance proposals filed this season, 271 went to a vote, while 105 were omitted, 104 were withdrawn, and 8 did not come to a vote for various reasons. The omission percentage was almost 22 percent, up from 15.6 percent in 2010 and 11 percent in 2009. One explanation is companies were able to exclude approximately 35 proposals this year by offering their own management proposal or taking board action, but many companies did not go as far as activists wanted.

So far, 90 governance proposals have received more than 50 percent of votes cast, down from 116 in 2010, and 149 in 2009. This downward trend is not surprising, given the declining volume of proposals.

Greater Support for Declassification

Among governance proposals, the biggest story during the 2011 spring proxy season was the greater support for shareholder proposals seeking board declassification. While this shareholder campaign didn't get much media attention before season, a diverse group of activists, including Florida's pension system, the Nathan Cummings Foundation, Harvard Law Professor Lucian Bebchuk, and retail investors have been pressing companies to drop staggered board terms and hold annual elections for all directors.

These resolutions averaged 73.5 percent support (based on votes cast "for" and "against"), up more than 12 percentage points from 2010, according to ISS data. In addition, declassification proposals won majority support at 35 firms.

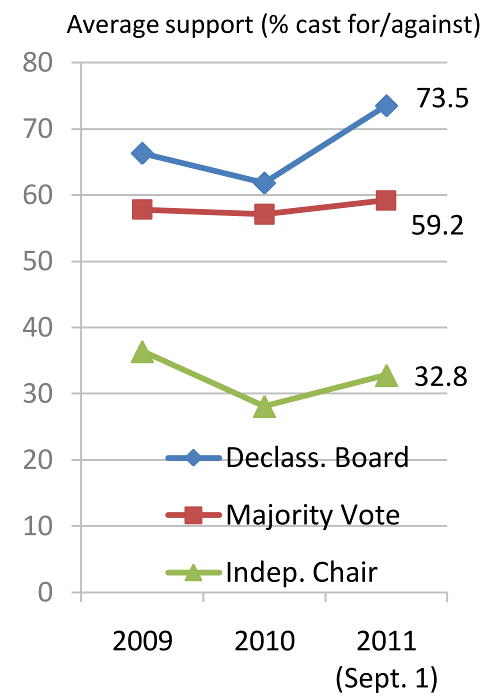
One explanation for the surge in support this year was that activists primarily targeted large-cap firms, which generally have greater institutional share ownership. Of the 38 companies where declassification proposals went to a vote this season, 23 were S&P 500 firms, and these resolutions won majority support at all but one large-cap company. The exception was Reynolds American, which has a 42 percent shareholder that votes with management. In 2010, only 10 of the 46 declassification proposals on the ballot were submitted at large-cap issuers, and 22 were filed at small firms outside the S&P 1500.

Another explanation is that more institutional investors have focused on this issue this year after a trio of recent Delaware court decisions upheld poison pills at companies with classified boards. After these unsuccessful challenges to pills, Bebchuk argued in a blog posting that declassification is an "antidote" to a poison pill, observing that such a defense "is powerful only as long as the directors supporting it remain in place."

As one would expect, declassification proposals have done very well at companies where management was neutral or made no recommendation, winning 97.6 percent support at Juniper Networks, 94 percent approval at St. Jude Medical, and 76.1 percent at Charles Schwab.

"We've been very pleased with the level of investor support for each of our proposals. The results thus far signal a clear investor preference for annual elections and moves to destagger boards. For several meetings this year, support levels have surpassed a supermajority," said Michael P. McCauley, senior officer for investment programs and governance at the Florida State Board of Administration.

Figure 17: Board Issue Proposals - R3000 Companies



Investors also have negotiated withdrawal agreements on declassification at a much higher rate than in past seasons. At least 15 companies have agreed to put the issue on the ballot this year or in 2012. This year, management proposals have passed at 44 of 47 firms. The exceptions were Eli Lilly, Principal Financial, and Barnes Group, which all have supermajority requirements. At Barnes, management recommended against its own proposal, which was put on the ballot after a shareholder resolution on this topic received 66.9 percent support in

2010. Despite management's opposition, this year's proposal still received 73 percent of votes cast, but failed to receive the necessary approval from two-thirds of the company's outstanding shares.

This season's vote results and proposal withdrawals are further evidence of the waning acceptance of classified boards at large companies. As recently as 2005, a majority (53 percent) of the S&P 500 index had staggered board terms. Today, just 30.8 percent of large-cap firms maintain classified boards, and another 3.6 percent are in the process of declassifying, according to ISS data.

While classified boards are more common at smaller companies, there has been a similar downward trend. In 2005, 59 percent of S&P 1500 firms had staggered board terms. Today, just 43.4 percent of those companies do, and another 3.2 percent are in the process of moving toward annual elections for all directors.

However, a few companies have used new state laws to resist shareholder demands for destaggering their board terms. Iowa, Indiana, and Oklahoma have passed laws that mandate classified boards. Oklahoma's 2010 law mandates classified boards until 2015. Indiana's 2009 law permitted companies to opt out during a limited period, and several companies have opted out retroactively. Ball Corp. used this law to exclude a declassification proposal last season, so shareholders tried a new strategy this year—filing proposals that ask Indiana companies to reincorporate to Delaware. This resolution won 43 percent support at Ball, a solid showing for a new proposal. Iowa, too, permitted companies to opt out of its classified board provision, which expires at the end of 2014.

Oklahoma-based Chesapeake Energy, which failed to implement a declassification proposal that received 86.7 percent support in 2009 and was featured in a recent *Wall Street Journal* article on Oklahoma's new law, may face a reincorporation proposal in the future.

It remains to be seen whether declassification proposals can repeat this strong showing in 2012. With fewer large-cap firms maintaining staggered board terms, there will be fewer corporate targets with significant institutional ownership where large majorities for declassification would be possible.

Renewed Interest in Majority Voting

After Congress removed a majority voting listing requirement from the draft Dodd-Frank legislation last summer, activists stepped up their efforts and submitted 82 resolutions--the most on any topic this year. After more than two dozen withdrawals, these resolutions went to a vote at 36 companies, and averaged 59.2 percent approval, up from 57.1 percent support in 2010, and 57.8 percent approval in 2009.

Majority voting proposals earned more than 50 percent of votes cast at 22 companies, which included eight S&P 500 firms. Among the highest votes were 99.6 percent at Spark Networks, 87.4 percent at Lorillard, and 82 percent at Gentex; management was neutral at all three companies. There also was 89.7 percent support at Wilshire Bancorp, where management endorsed the proposal. Notwithstanding management opposition, majority voting also received 79.4 percent approval at Vornado Realty and 77.5 percent at Pioneer Natural.

In addition, the United Brotherhood of Carpenters and other investors withdrew at least 35 proposals, usually after companies agreed to adopt this reform, while Florida and California's pension systems obtained additional commitments through letter-writing campaigns. The Council of Institutional Investors also has urged companies to adopt majority voting. In addition, 18 management proposals on majority voting have won investor approval this year, and it appears likely that investors may see more management proposals on this topic in 2012, especially at small-cap firms.

Improvement for Independent Board Chair Proposals

In a surprising showing, independent board chair proposals at Russell 3000 companies averaged 32.8 percent support at 23 companies, an improvement over last year's 28.1 percent showing and slightly below the 36.4 percent average in 2009, the previous high water mark for this topic. In addition, a proposal at non-Russell 3000 company, Cedar Fair L.P. received 81.1 percent support during a proxy fight. This year's rebound may be a result of more selective targeting by proponents; in 2010, 59 proposals were filed and 41 went to a vote.

In addition to Cedar Fair, independent chair proposals won majority support (based on votes cast) this season at Aetna, Moody's, and Vornado Realty after similar proposals fell short in the past.

At Aetna, there was 51.4 percent support this year, as compared with 33.5 percent approval in 2009 and 29.8 percent in 2008. It appears that the health insurance company's financial performance helped persuade investors to embrace this change. The company's one- and three-year total share returns (TSR) of negative 3.62 percent and minus 19.03 percent, respectively, underperformed its industry peers' TSRs of 12.64 percent and negative 0.59 percent, respectively. The company has a presiding director, who does not have the authority to call meetings of independent directors.

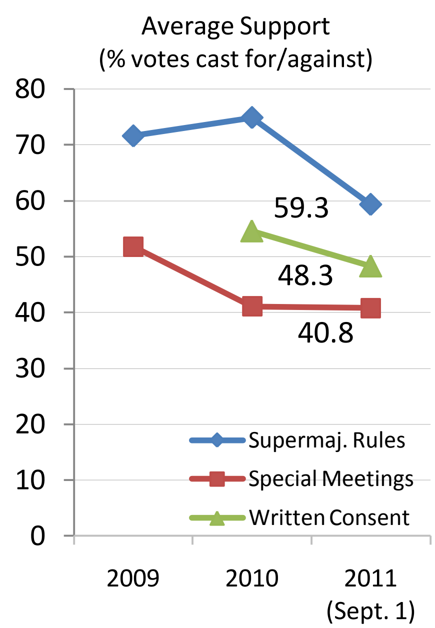
At Moody's, there was 56.6 percent support this year, a significant increase from the 33.4 and 30.8 percent votes for independent chair proposals in 2010 and 2009. It appears that this year's vote was a reaction to the rating company's lagging share performance, which has trailed its peers over the past one, three, and five years.

At Vornado, there was 50.7 percent support, up from 41 percent in 2010. While the real estate investment company has posted good performance, management had failed to implement two majority-supported shareholder proposals from 2010.

Cumulative voting proposals, which primarily have been filed by investor activist Evelyn Y. Davis, averaged 29.9 percent approval at 22 companies, up from 27.2 percent in 2010. The best showing for this topic was 41.5 percent support at Home Depot.

CEO succession planning received a significant amount of press attention before this proxy season after the sudden ouster of Hewlett-Packard's chief executive in August 2010 and the continuing health problems of Apple founder Steve Jobs. The Laborers' International Union of North America planned to file almost a dozen proposals, but withdrew most of them or reached settlements before filing. Just two resolutions went to a vote, receiving 30.1 percent support at Apple and 23.9 percent at Kohl's.

Figure 18: Takeover Defense Proposals – R3000 Companies



Less Shareholder Support For Takeover Defense Limits

One surprise this season is that there were fewer proposals to repeal supermajority voting requirements, and these resolutions did not match their season-leading support levels of 2010. These resolutions averaged 59.3 percent support at 15 companies, down from 74.3 percent at 29 companies in all of 2010. One explanation for the smaller volume of investor proposals this season was that companies were able to omit 16 proposals; in most cases, issuers offered their management proposals on this topic.

This season's results include a 98 percent vote at Prudential Financial, where management supported the proposal, and 78.3 percent at Sprint Nextel. There was just 9.8 percent support at Google, where insiders have a 58 percent voting stake, and other investors presumably concluded that existing supermajority rules help protect their interests. At Southwest Airlines, a proposal filed by shareholder activist John Chevedden won 65.3 percent support, but the company asserted that this resolution was not properly presented for a vote.

While there were fewer shareholder proposals seeking to repeal supermajority provisions, there was a spike in management proposals on this topic. As of June 30, 61 management proposals had gone to a vote, up from 41 during the same period last year. All but seven of this year's proposals have passed. Most of the failures were at companies, such as Eli Lilly, that have an 80 percent of shares outstanding vote requirement. Overall, the prevalence of supermajority rules at large cap firms has been declining. Just 35.5 percent of large-cap firms now have supermajority requirements for a merger or business combination, while 53.4 percent require such approval for bylaw or charter amendments, according to ISS GRId data.

Also this year, investors filed 50 proposals that seek the right of investor groups to call special meetings; most proposals called for a 10 percent ownership threshold. Companies were able to omit 12 proposals; in most cases, management offered competing proposals with higher (such as 25 percent) thresholds. Twenty-nine shareholder proposals went to vote at Russell 3000 companies and averaged 40.8 percent approval, which is slightly below their 2010 showing. Five 2011 proposals won a majority of votes cast; among them were resolutions at NYSE Euronext, NV Energy, and Home Depot. This topic generally received less support at companies, such as Amazon.com, DuPont, and Office Depot, that already permit shareholders to call special meetings, but have set a higher ownership threshold than sought by activists.

Investors also approved 21 management proposals on this topic and 18 resolutions earned more than 87 percent support. However, there was just 64 percent approval at Mattel; its proposal included a 15 percent net-long position requirement, which some investors viewed as too onerous.

Shareholder proposals seeking the right to act by written consent did not do as well this season as last year when this topic reappeared on proxy ballots after more than a decade absence. Written consent proposals averaged 48.3 percent approval at 33 companies, down 6 percentage points from 2010. This topic received majority support at 12 companies; there was at least 60 percent approval at Devon Energy, Staples, Liz Claiborne Inc., NYSE Euronext, and R.R. Donnelley & Sons. The lowest result was 23 percent support at Kohl's, which has a full array of other shareholder rights, including majority voting, a declassified board, and a 10 percent special meeting threshold.

More Investor Support For E&S Proposals

The average investor support for shareholder resolutions on environmental and social (E&S) issues continues to rise.

During the spring proxy season, there was a 20.6 percent average approval rate for these proposals, the first time this support level had reached the 20 percent mark. This average compares with 19.3 percent at the same time a year ago and 18.1 for all of 2010, according to ISS data. By contrast, the average support for E&S proposals was just 8.7 percent a decade ago.

This year's vote average includes five investor proposals that received majority support (based on "for" and "against" votes), a new record for E&S issues. These proposals include:

- KBR: a request to include sexual orientation in the company's nondiscrimination policy (61.7 percent approval);
- Tesoro: a request for a report on refinery safety (54.3 percent support);
- Sprint Nextel: a request for a report on political contributions (53.3 percent);
- Ameren: a request for a report on coal combustion waste (52.7 percent); and
- Layne Christensen: management supported a shareholder's request for a sustainability report (92.8 percent).

Additionally, a proposal at Energen requesting a report on the environmental impacts of the hydraulic fracturing method increasingly used in natural gas production won 49.5 percent approval, barely missing receiving majority support, while three proposals requesting a report on political contributions (at Halliburton, R.R. Donnelley, and Lorillard) earned more than 45 percent support.

Political Contributions

As in recent years, political contribution-related proposals accounted for just under a quarter of the proposals filed, and just under a third of the resolutions voted on. What was notable this year was the much greater variety of approaches to this issue following the U.S. Supreme Court's *Citizens United* (2010) decision, which removed caps on independent corporate spending in federal elections.

As in earlier proxy seasons, though, the largest part of the political contributions campaign were the resolutions from a seven-year-old effort coordinated by the Center for Political Accountability (CPA), which ask for reports on corporate political spending and policies, including spending funneled through trade associations. Thirty-two resolutions in the CPA campaign came to votes this year.

This year, the average support for political contributions proposals was 32.5 percent, up from 30.4 percent for similar proposals in 2010. This average doesn't include a low vote of 5 percent at Sears, which is a controlled company, proposals from several long-running initiatives by activist investor Evelyn Y. Davis, which are different in scope, and a proposal at Home Depot asking for an annual advisory vote on "corporate electioneering."

Among the new variations in proposals were the resolutions coordinated by Walden Asset Management that were directed at companies that serve on the board of the U.S. Chamber of Commerce. In addition to requesting reports on political spending, those proposals asked the companies to discuss the risks and responsibilities associated with serving on boards of and paying dues to trade organizations when positions of the association contradict the company's own positions. The proponents were particularly concerned about the U.S. Chamber's opposition to legislation to mitigate climate change. The resolution was initially filed at seven companies, but after a mix of withdrawals and technical issues, it came to votes only at IBM and PepsiCo, receiving 31.4 and 11 percent support, respectively. In addition to these proposals, Walden also raised the issue from the floor at several other annual meetings this year and plans to continue pressing this matter in 2012.

Other proposals targeted corporate support for ballot initiatives during the 2010 elections. A proposal asking for a report on political contributions in light of the reputational risks arising from corporate contributions given to a group that supported an openly antigay gubernatorial candidate in Minnesota was filed at Best Buy, Pentair, Target, and 3M. Withdrawal agreements were reached at all but 3M, where the proposal received 35.8 percent support. Another proposal voted on at Occidental Petroleum and Valero focused on the companies' corporate support for Proposition 23, the campaign in California that would have suspended a state law to regulate carbon emissions. These proposals earned 30.6 and 34.8 percent support, respectively.

By contrast, a new proposal at Home Depot from NorthStar Asset Management that sought an annual shareholder vote to ratify political expenditures anticipated in the next fiscal year received only 5 percent support. The CPA has specifically opposed that approach.

In addition to the standard CPA proposal, AFSCME filed a new proposal that requested a report on "grassroots lobbying" and corporate funds given to trade associations and other third parties that are used for political purposes. These proposals averaged 24.2 percent support at five companies (the average was lowered by the 8 percent vote at Prudential Financial, the only vote below 25 percent).

Environmental Issues

Environmental proposals were about as prominent during this year's E&S proxy season as political contribution resolutions and even more varied.

The most eye-catching results involved the second year of a campaign coordinated by the Investors Environmental Health Network to ask companies to report on the implications of their use of hydraulic fracturing to tap natural gas reserves. These proposals went to a vote at five companies--Energen, Chevron, ExxonMobil, Ultra Petroleum, and Carrizo Oil & Gas--and averaged 40.7 percent support, up more than 10 points from 2010. The votes came in the wake of increasing regulatory and public attention to an issue many investors were barely familiar with 18 months ago.

Another notable aspect of this proxy season was the increased shareholder attention to the risks related to the use of coal, which is now going beyond concerns about climate change. Activists filed a new resolution asking utilities to report on the financial risks of coal reliance, which ultimately came to votes at four companies. Only one of those resolutions got better than 10 percent support--a 31.4 percent vote at FirstEnergy-- as investors appeared to conclude that some of the targets were already implementing this resolution by providing considerable information on the issue, even if the underlying concern remained. In a related campaign, three resolutions that asked utilities to disclose more about how they are approaching the issue of coal combustion waste fared better, winning majority support at Ameren.

Additionally, the Sierra Club filed a new resolution at Dominion Resources asking for a report on mountain-top coal mining that received 9.3 percent support.

The number of resolutions specifically focusing on climate change appears to have fallen this year, from 41 filed in all of 2010 to 34 filed so far in 2011. After many withdrawal agreements, 12 had come to votes by June 30, down from 19 voted on in all of 2010. Eight of those were part of the now familiar campaign requesting companies to adopt quantifiable metrics for greenhouse gas (GHG) emissions. Those votes averaged 18.6 percent support. Among the other climate change proposals that came to votes were second-year resolutions asking for reports from Chevron and ConocoPhillips on the financial risks of climate change; those votes remained low, at under 8 percent. Overall, climate change-related proposals averaged 17 percent support--as compared with 21.1 percent in all of 2010—and it is unlikely that any of the 2011 climate change-related measures listed above will reach the levels seen in 2010.

In addition to the 11 proposals voted on from climate change activists, shareholders considered four from pro-business groups that are skeptical about the severity of the issue. These resolutions averaged only 3.2 percent approval; the best showing was 6.5 percent support for a resolution on climate-related lobbying at Duke Power.

Among other environmental issues, support for resolutions asking companies to report on oil sands development remained strong at ConocoPhillips and ExxonMobil, averaging 27.5 percent.

Sustainability Questions

The number of resolutions proposed requesting reports on sustainability has fallen by about half, to 22, so far in 2011 compared to end of year 2010 figures and a large batch of withdrawals left only seven to go to a vote. These proposals averaged a solid 29.4 percent approval rate, not including the management supported proposal at Layne Christensen, which received 92.8 percent support. However, a new proposal from the Laborers' International Union asking companies to link sustainability metrics to executive compensation got off to a slow start. Of the four proposals that came to votes, the best showing was 6.9 percent support at Sempra Energy. Additionally, the boards at two of the targets, Chevron and Equity Residential, argued in their proxy statements that they had already recently tied their compensation to sustainability.

Sexual Orientation Nondiscrimination

The campaign to get companies to amend their nondiscrimination statements to include sexual orientation and gender identity continued at about the same pace as in recent years (28 proposals filed), as always with a high number of withdrawals. For the nine resolutions that came to votes, the average support was 30.2 percent, three points below the average support in 2009 and 2010, despite this year's 61.7 percent vote at KBR, the highest ever social issues vote result.

Health and Safety Proposals

A new AFL-CIO campaign this year asking oil companies to report on their actions to reduce the risk of workplace accidents received varied levels of support. At Tesoro, where a recent refinery accident had resulted in fatalities, and Valero, where disclosure was limited, the proposals received 54.3 and 43.3 percent approval, respectively. At Conoco and Marathon, the proposals received much lower support of 7.8 and 7.4 percent, respectively. At Chevron, an individual investor filed a proposal that asked for a report on offshore oil wells and safety measures; this resolution received 8.6 percent support.

Recycling

So far this year, investors have voted on three proposals that deal with different aspects of corporate recycling. A repeat proposal at Starbucks, which asked for beverage container recycling goals and a report, received 8.1 percent support. A new proposal at McDonald's--asking for a report on beverage container recycling and information on the company's use of polystyrene beverage containers--received 29.3 percent support. Another new proposal was filed at Target; this proposal asked for a report on minimizing the environmental impact of electronics recycling and earned 30.8 percent support.

Several issues received notably low votes this spring. A revived church-led campaign to get four drug companies to implement a pharmaceutical price restraint policy averaged only 3.2 percent support. Animal welfare-related proposals continue to draw limited support, with just 4.8 percent average approval, as did resolutions on tobacco issues, which averaged 2.4 percent support.

Comparisons With 2010

So far, ISS has tracked 348 E&S proposals proposed for 2011 meetings, and while a few more will undoubtedly surface, it is unlikely that the totals will hit the 384 filed in all of 2010. At 124, the number of negotiated withdrawal agreements is also well below the record of 146 set in 2010. However, the SEC has allowed companies to omit 51 resolutions so far, which already has surpassed last year's total of 50.

Advisory Votes Lead To Less Dissent on Directors

With the Dodd-Frank Act mandating advisory votes on compensation at most U.S. companies this year, shareholders were provided with an alternative avenue to express their views on corporate pay programs. Investors may now vote against management "say on pay" proposals in lieu of withholding support from pay panel members. The advent of "say on pay" has contributed to a significant decline in shareholder opposition to director elections at U.S. firms in 2011.

Although the vast majority of directors at U.S. companies were elected with more than 90 percent shareholder support, 45 directors failed to win a majority of votes for their election this year, according to ISS data on meetings through Sept. 1. During the same periods in 2010 and 2009, 91 and 93 directors, respectively, failed to garner majority support. Ferro Corp., Fred's Inc., Healthcare Services Group Inc., IRIS International Inc., and Vornado Realty Trust each had more than one director receive majority opposition. Firms in the health care sector suffered the greatest number of failed elections, followed by companies in the industrials sector, and then those in the financial services, TMT, and retail sectors.

This season, poor attendance was the most common contributor to failed director elections. According to ISS data, 17 directors received more than 50 percent shareholder opposition after it was reported that they did not attend at least 75 percent of board and/or committee meetings. At Taleo, a Delaware-based talent management software solutions provider, a director received just 21.4 percent approval, one of the lowest levels of support this year. Investors of CoStar Group withheld a majority of votes from a director amid continuing attendance concerns. In 2010, that same nominee garnered only 40.5 percent support.

Another common driver of failed director votes was not putting a poison pill to a shareholder vote. The entire nine-member board of IRIS International received majority investor opposition as the company did not submit a pill adopted in 2010 for shareholder ratification at this year's meeting. A director at Hutchinson Technology also received a majority "withhold" vote under similar circumstances.

Shareholders have also registered discontent against boards that did not address underlying reasons behind failed director elections at the prior year's shareholder meeting. At Fred's Inc., two directors failed to gain majority support this year after the board did not seek shareholder approval to renew a poison pill and did not adopt a majority voting standard for board elections. This unresponsiveness contributed to majority shareholder opposition to all the company's nominees last year.

Similarly, the lack of responsiveness by boards to majority-supported shareholder proposals continues to trigger high levels of shareholder dissent. All three trustee nominees at Vornado Realty Trust received majority investor opposition after the board did not implement majority-backed shareholder proposals to adopt a majority vote standard for the election of trustees and to declassify the board. The trustee nominees at Vornado's 2010 annual meeting also garnered significant opposition after the board failed to act on an earlier shareholder-approved proposal to require a majority voting standard. Shareholders also opposed the election of two directors at Ferro Corp. after the board did not amend the company's code of regulations to provide that the company opt out of the Ohio Control Share Acquisitions Act. This amendment was the subject of a shareholder proposal that won majority support at the firm's 2010 annual meeting.

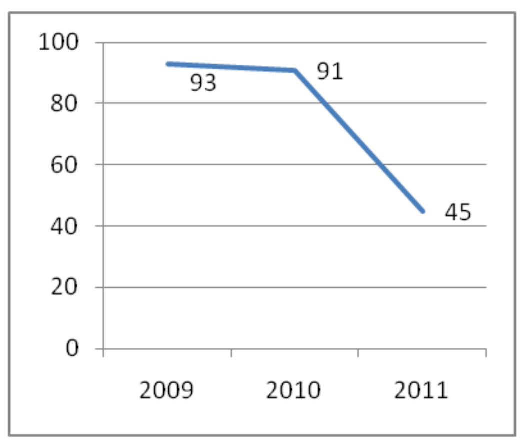
Only a handful of failed director elections appear to have been driven by lack of board or committee independence. At Healthcare Services Group, there again was majority opposition to directors over the board's not establishing a majority independent board. At HMS Holdings Corp., holders of a majority of shares withheld votes from the company's former CEO, who sits on each of the key board committees.

Holding an excessive number of directorships contributed to three failed elections in 2011 but appears to have been the sole factor at just one company, HSN Inc. Overboarded director nominees at Brookdale Senior Living and Hersha Hospitality Trust who failed to win majority support also had poor attendance records.

Unlike 2010, when concerns related to executive compensation were a factor in nearly one-third of failed director elections, compensation-related concerns were a factor in only two failed elections in 2011. At TASER International, the sole member of the compensation committee standing for election received 40.4 percent support after that company conducted a non-shareholder-approved option exchange. For the second straight year, a member of Stewart Information Services Inc.'s compensation committee received less than majority support. In recent years, Stewart's CEO's compensation has increased sharply amid poor shareholder returns.

The emergence of "say on pay" as an alternative to votes against compensation committee members may be reducing votes against directors in general. The average level of support for Russell 3000 directors has climbed to 95 percent from 94 percent in 2010 and 93 percent in 2009.

Figure 19: Number of Directors Receiving Less Than 50 Percent Support



Drivers of High Opposition Votes at S&P 500 Firms

While four directors at two S&P 500 firms (Vornado Realty and Nabors Industries) had majority dissent, almost 60 directors at large-cap firms faced more than 30 percent dissent. More than half of these directors who received high opposition votes at S&P 500 companies had not acted on majority-supported shareholder resolutions.

All members of Allstate's 11-member board drew more than 30 percent negative votes after the board did not implement a majority-supported shareholder proposal to lower the ownership threshold to call a special meeting from 25 to 10 percent. Shareholder proposals seeking a 10 percent threshold have received a majority of votes cast for two consecutive years. There was significant opposition to directors despite management's submission of a proposal to allow holders of not less than 20 percent of the company's outstanding shares to call a special meeting. For the same reason, eight of the 13 directors at Marathon Oil garnered less than 65 percent support. While the board has proposed to lower the special meeting threshold from 25 to 20 percent, shareholders did not appear satisfied with that response to their request for a 10 percent threshold.

At Ball Corp., a director nominee received only 64.3 percent support after the board did not act on a shareholder proposal to submit the company's poison pill to a shareholder vote. The board's not opting out of Indiana’s classified board provision also appears to be another factor behind this high opposition level. Shareholder proposals to declassify the board have won majority support in 2005, 2006, 2008, and 2009. By not opting out of the Indiana law, the company has, in effect, installed a perpetually classified board.

Corning, Pioneer Natural Resources, Vornado Realty, and FirstEnergy are other firms where investors expressed significant opposition against at least one director nominee for ignoring majority-supported shareholder proposals.

This year's board election at Cablevision Systems was also noteworthy as all five nominees elected by holders of Class A common stock received high levels of opposition. Investor concerns over the company's corporate governance structure, compensation practices, and lack of responsiveness to shareholder views appear to have spurred the protest votes. In 2010, the firm's compensation committee members drew majority withhold votes for entering into new employment agreements that contained modified single-trigger change-in-control provisions and non-performance-based awards.

Shareholders also withheld a high number of votes from all five nominees at Stanley Black & Decker after the board did not address the underlying issues that triggered a majority of shareholders to withhold support from one of the nominees at the last annual meeting. In 2010, director Virgis W. Colbert, chairman of the compensation committee, received only 46.4 percent support. The concerns expressed at last year's meeting involved the board's failure to heed a majority-backed shareholder proposal to declassify the board and an agreement entered into with the company's executive chairman that contained guaranteed multiyear equity grants.

Director nominees who serve as affiliated outsiders on key board committees also drew more than 30 percent negative votes at Anadarko Petroleum; BB&T; Becton, Dickinson and Co.; C.H. Robinson Worldwide; Franklin Resources; PNC Financial Services Group; and Whole Foods Market.

Poor meeting attendance and directors serving on too many outside boards were other reasons that drew high opposition votes at large-cap firms. Companies in the energy and financial services sector topped the list of S&P 500 companies that had high levels of shareholder opposition to their boards (32 percent) followed by firms in the industrials and TMT and media sectors (16 percent).

Figure 20: Significant Opposition at S&P 500 Companies

More than 50% Opposition	Governance Issues
Nabors Industries Ltd.	Failure to act on a shareholder proposal to declassify the board
Vornado Realty Trust	Failure to act on shareholder proposals to declassify the board and adopt majority voting
40--50% Opposition	**Governance Issues**
Stanley Black & Decker Inc.	Lack of responsiveness to a majority vote against a director in 2010; problematic compensation practices
Allstate Corp.	Failure to fully implement a shareholder proposal to allow 10 percent of shareholders to call special meetings; problematic compensation practices
LSI Corp.	Overboarded director
Harley-Davidson Inc.	Attendance
PPL Corp.	Attendance
Invesco Ltd.	Overboarded director; problematic compensation practices
PNC Financial Services Group Inc.	Affiliated director on key board committees
Pioneer Natural Resources Co.	Failure to act on a shareholder proposal to adopt majority voting
Becton, Dickinson and Co.	Affiliated director on a key board committee
Corning Inc.	Failure to act on a shareholder proposal to reduce supermajority vote requirements
Dell Inc.	Attendance
30-40% Opposition	**Governance Issues**
Cablevision Systems Corp.	Lack of responsiveness to a majority vote against directors in 2010; problematic compensation practices
Hewlett-Packard Co.	Failed to lead the process for board appointments
Marathon Oil Corp.	Failure to fully implement a shareholder proposal to reduce the threshold required for shareholders to call special meetings; problematic compensation practices

C.H. Robinson Worldwide Inc.	Affiliated director on key board committees
Ball Corp.	Failure to act on a shareholder proposal to submit the company's poison pill to a shareholder vote; failure to opt-out of Indiana law mandating classified boards
FirstEnergy Corp.	Failure to act on shareholder proposals to adopt majority voting and to reduce the threshold required for shareholders to call special meetings
Illinois Tool Works Inc.	Attendance
Electronic Arts Inc.	Overboarded director
Anadarko Petroleum Corp.	Affiliated director on a key board committee
M&T Bank Corp.	Overboarded director
Whole Foods Market Inc.	Affiliated directors on key board committees
Franklin Resources Inc.	Affiliated director on a key board committee
PPL Corp.	Problematic compensation practices
BB&T Corp.	Affiliated director on key board committees
Wells Fargo & Co.	Affiliated director on key board committees

Resignation Policies

As in past proxy seasons, most of this year's majority-opposed directors serve at smaller companies that have plurality vote standards and lack resignation policies for board members who fail to win majority support. However, resignation policies were triggered at several companies this season, including IRIS International, where all nine board members failed to earn majority support after adopting a poison pill without shareholder approval. The individual directors submitted their resignations, but the board declined to accept them, and reaffirmed their position that submitting the firm's poison pill to a shareholder vote was not merited.

A resignation policy also was triggered at HSN against director Gregory Blatt, who is CEO of the company's former parent, IAC/InterActiveCorp.; the opposition apparently reflected concern that he sits on too many other boards. While the board rejected Blatt's resignation, HSN said that Blatt would reduce his other board commitments from three to two after IAC acquires another company, according to Bloomberg News.

At Synovis Life Technologies, the company's former CEO, Karen Gilles Larson, received majority opposition amid investor concerns that she was not sufficiently independent to serve on key board committees. The board announced that Larson would step down from these committees after replacements were identified.

Proxy Contest Volume Falls, Activism Continues Behind the Scenes

For the second straight year, the number of contested meetings at U.S. companies fell sharply. Only nine contested meetings went to a shareholder vote during the first half of 2011, compared to 14 and 25 for the same periods in 2010 and 2009, respectively. However, the number of public settlements and anecdotal evidence of behind-the-scenes agreements suggests that the level of shareholder activism continues to be high.

Whereas governance and operating reforms historically dominated dissidents' agendas in recent years, a hot M&A market fueled by strong balance sheets and the search for earnings growth contributed to the resurgence of the "sell the company" platform in 2011, including at Mentor Graphics and Fisher Communications, where shareholders supported dissident nominees. Even a pending acquisition failed to forestall a consent solicitation at Zoran Corp., where dissident Ramius ultimately won three of seven board seats. Further, while not a central component of the dissident's platform at Ameron International, that company agreed to an acquisition two months after the lone dissident nominee was elected to the board.

Notable settlements included Charles River Laboratories International and Iron Mountain, which, among other things, added new directors to the board and formed special committees dedicated to exploring strategic alternatives. Additionally, the pending acquisition of NYSE Euronext by Deutsche Bourse AG was interrupted by an unsolicited offer by NASDAQ OMX Group and IntercontinentalExchange Inc. The offer was ultimately withdrawn amid opposition from NYSE's board and regulators' blunt statements that the deal would not receive regulatory approval, though NYSE shareholders ultimately received a special dividend of $2.00 in addition to the all-equity merger consideration valued at approximately $36.90 per share.

Overall, investors won at least one board seat at four of the nine contests that went to a shareholder vote. Dissidents sought board control at only one firm, Zoran Corp.

Robert Yates, Mason McAllister, Valerie Ho, Sean Quinn, and Carol Bowie contributed to this report.

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