

August 6, 2015

**ISS Releases 2016 Policy Survey**

Institutional Shareholder Services Inc. (“ISS”) released its annual Policy Survey two days ago. As usual, the Policy Survey seeks responses from institutional investors, issuers, directors and other market constituents on a wide range of corporate governance matters and is generally a good indicator of the areas for which ISS is considering a policy change for voting recommendations in the forthcoming proxy season. Below is a brief summary of topics on which ISS is seeking input for 2016 that may be of particular interest to publicly traded Maryland companies.

Proxy Access: Proxy access proposals were extremely popular and successful in 2015, and we anticipate similar results in 2016. If a proxy access proposal is approved and the company in response implements a proxy access policy with restrictions not contained in the proposal, ISS is asking which restrictions are viewed as material enough to question the sufficiency of the board’s response. ISS may decide that proxy access proposals must be implemented substantially as approved or it will recommend against future director nominees. Such a policy change could effectively force a company to choose between implementing its own policy, for which the board can determine all the terms, or wait and see whether the company receives a proposal, in which case the company may need to implement the policy substantially as submitted by the shareholder(s), if it is approved. This is important because proxy access policies are complex and contain many important variables.

Independent Director Compensation: ISS is asking about equity compensation for independent directors. ISS may be seeking to determine whether certain types of equity compensation (such as options) or performance-based compensation may overly align directors with management or create inappropriate incentives.

Unilateral Board Amendments to Organizational Documents: ISS is asking how long directors should be penalized for unilaterally amending the charter or bylaws in a manner that “materially diminish shareholders’ rights” -- specifically, whether directors should be held accountable only at the next annual meeting of shareholders or for some longer period of time. Additionally, ISS is asking which types of unilateral amendments are most egregious. Any change in this area would be of particular importance to publicly traded Maryland companies as the boards of these companies generally have the exclusive right to amend the bylaws and, in certain cases, to unilaterally self-classify the board and take other actions. Penalizing directors of Maryland corporations for more than one annual meeting could potentially chill their willingness to take full advantage of such powers.

Pre-IPO Bylaw Amendments: ISS is asking for views on “evaluating board accountability” for pre-IPO bylaw amendments that “materially diminish shareholders’ rights before the company becomes publicly traded.” We are puzzled by ISS’s concern in this regard as it seems to imply that investors are not able to evaluate for themselves any and all charter and bylaw provisions.

Externally Managed Entities and Say-on-Pay: ISS is inquiring about externally managed entities that have a Say-on-Pay vote but may only offer limited information on executive compensation because officers of externally managed entities are customarily employed and compensated by the manager. This indicates ISS may start expecting externally managed entities to provide more complete disclosure about officer compensation, even if such compensation is paid by the manager. This policy is important because many externally managed entities are Maryland REITs. It is also important to Maryland REITs that are not externally managed, because many will have peer group members that are.

Non-GAAP Metrics: ISS is asking about the use of adjusted or non-GAAP metrics in incentive programs. Any policy change here would be important to REITs as they typically rely on metrics such as Funds from Operations and Adjusted Funds from Operations. However, we anticipate any change would recognize that these metrics have long been viewed as non-controversial and commonplace among REITs.

In addition, ISS is also seeking views on net-operating-loss shareholder rights plans, “overboarding” and a cooling-off period for directors who are former CEOs or advisers.

The release of the Policy Survey is the first step in ISS’s annual policy update process. The remaining steps for the coming proxy season are likely to occur as follows:

- Policy Survey Closes – September 4, 2015
- Policy Survey Results Released – Late September
- Proposed Updates to Proxy Voting Guidelines – October
- Open Comment Period for Proposed Guidelines – October
- Final Updates to Proxy Voting Guidelines Released – November

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We urge you to review the Policy Survey. Our colleagues and we would be glad to review the potential implications of the Survey for your company’s current corporate governance.

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