

## **Relative Financial Results to be Included in ISS Reports**

ISS [announced](#) on November 8th that proxy research reports published after February 1, 2017 will include a standardized comparison of the company's CEO pay with a relative financial performance ranking versus peers as measured by multiple financial metrics including return on equity, return on assets, return on invested capital, revenue growth, EBITDA growth, and growth in cash flow from operations.

The relative financial metric results will be used solely in ISS's qualitative pay-for-performance analysis, at least for 2017. The quantitative pay-for-performance screen will not change for 2017 and will continue to be based on relative and absolute total shareholder return (TSR).

ISS noted that both investors and issuers have been supportive of ISS using metrics beyond TSR for pay-for-performance evaluations. In fact, 79% of investors and 68% of issuers supported the use of the additional metrics in ISS's 2017 global benchmark policy survey.

### **ISS's announcement included the following specific information related to the changes:**

- **New Financial Metrics.** ISS reports published after February 1, 2017 will include a standardized table comparing the company's performance across six financial metrics relative to its ISS-defined peer group. The metrics will be three-year ROIC, ROA, ROE, revenue growth, EBITDA growth, and growth in cash flow from operations, along with TSR. The weight of each metric will vary by industry, but ISS has not yet disclosed the exact weightings.
- **Overall Relative Financial Performance Metric.** ISS will produce an overall relative financial performance metric to be compared against relative granted pay, to produce a numeric result indicating alignment between three-year financial performance and three-year pay.
- **Relative Degree of Alignment Test.** The new financial performance evaluation test, along with the long-implemented Relative Degree of Alignment test, will only apply to companies with two full fiscal years of trading data. The RDA test will continue to compare relative TSR to relative CEO compensation over one- and three-year periods.
- **Peer Group Submission Window.** The peer submission window for U.S. and Canadian companies will run from November 28<sup>th</sup> to December 9<sup>th</sup>.

### **What should issuers do now?**

- **Monitor New ISS Financial Metrics.** ISS noted that more information will be available in the coming weeks, through FAQs and other documents, including presumably the exact weighting of financial metrics for each industry. In the meantime, issuers should consider calculating the ISS-selected metrics for themselves and peers to gain a preliminary understanding of where they will rank under the new test.
- **Enhance CD&A Disclosure Regarding Various Metrics.** ISS announced the market-wide use of six financial metrics that will be applied under their refined qualitative analysis. These six metrics are not necessarily widely used or even appropriate measures for all industries or companies. As such, issuers should now start refining CD&A disclosure about what financial metrics are most important to their business and how they are performing against these measures. Issuers might also consider affirmatively disclosing why some of ISS's metrics might not be as important or reflective of industry or company performance.

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- **Peer Group Submission Window.** Companies that made changes to the peer groups used for benchmarking 2016 CEO pay should consider submitting their revised peer groups to ISS through ICS' Governance Analytics platform. Companies can reach out to ISS to obtain login credentials if they do not already have them. If your company did not make any changes to your peer group for 2016, there is no action to be taken. Additional instructions for companies detailing the peer submission process during this window are expected in the coming days.

## Some remaining questions include:

- What are the specific weightings by industry?
- How much will these metrics impact ISS's qualitative review analysis?
- Will ISS consider company-specific circumstances that make certain metrics and the industry weightings inappropriate?
- How will ISS account for M&A? Will companies who have made significant acquisitions/divestments automatically fare well/poorly on the revenue, EBITDA, and CFFO growth metrics?
- Will companies with structurally lower ROE/ROIC/ROA than peers be penalized even if management has performed well in improving these metrics?
- Will these metrics and the composite score be added to ISS's formulaic quantitative analysis in the future without consideration of a company's specific circumstances?

## About CamberView

*CamberView Partners is the leading provider of independent, investor-led advice to public companies on how to successfully manage investor engagement, contested situations and complex and challenging corporate governance issues. We advise company executives and boards on a wide range of events including contested merger situations, hedge fund activism, director elections, compensation matters, difficult shareholder proposals, sustainability and more. CamberView helps its clients succeed with their investors by providing insight into the investor's perspective, explaining how investors will respond to the company's proposals, and creating successful proactive strategies for investor engagement.*

## CamberView Team

### **Abe Friedman**

415.906.6501

[abe.friedman@camberview.com](mailto:abe.friedman@camberview.com)

### **Chris Wightman**

415.906.6504

[chris.wightman@camberview.com](mailto:chris.wightman@camberview.com)

### **David Martin**

212-235-2920

[david.martin@camberview.com](mailto:david.martin@camberview.com)