



Post #37: ISS’s Say on Pay Vote Recommendations Surprisingly Similar to Last Year

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Heading into this recently past proxy season, experts speculated that ISS might recommend “against” say on pay proposals among the energy industry at a higher rate compared to last year assuming the dramatic decline in stock prices, driven by the drop in commodity prices over the past year, would give ISS the ammunition it needed to roil against common oil and gas industry pay practices it tends not to like, such as:

- Greater use of discretion in incentive plans
- Greater portion of time-based restricted stock in LTI plans
- Lack of negative TSR provisions in LTI performance plans
- More generous change in control severance provisions

Using data as of June 11th, 2015, ISS vote recommendations by Russell 3000 energy segments are shown in the table below.

| Energy Segment | 2015 | | | 2014 | | |
|------------------------------------|--------|---------|-------------|--------|---------|-------------|
| | # Cos. | ISS FOR | ISS AGAINST | # Cos. | ISS FOR | ISS AGAINST |
| Oil & Gas Drilling | 14 | 86% | 14% | 14 | 86% | 14% |
| Oil & Gas Equipment & Services | 34 | 79% | 18% | 42 | 88% | 12% |
| Oil & Gas Exploration & Production | 64 | 81% | 19% | 69 | 81% | 19% |
| Oil & Gas Refining & Marketing | 11 | 100% | 0% | 16 | 94% | 6% |
| Oil & Gas Storage & Transportation | 6 | 83% | 17% | 6 | 83% | 17% |

While ISS has recommended “against” say on pay for a larger percentage of energy companies than the broader general industry (17% vs. 11%, respectively) I was surprised to find that ISS has recommended “against” the same percentage of upstream companies’ say on pay proposals as 2014. In fact, most segments are tracking towards similar ISS vote recommendations as last year. Among the equipment and services companies, so far ISS has recommended against say on pay for only one more company than it did in 2014.

For those that received “against” say on pay recommendations from ISS to date, practices mentioned above were often cited in conjunction with “high” or “medium” concern levels, frequently identified by ISS’s “relative degree of alignment” and “pay-TSR alignment” tests (for more information on ISS’s tests refer to our [client alert](#) from December 2014). Often ISS also noted pay increases or above-target incentive payouts during a period of declining performance in its qualitative reviews.

Those energy companies (across all segments) that have received “against” recommendations to date also have experienced a greater decline in TSR compared to those that received “for” say on pay recommendations.

| 2015 ISS Say on Pay Recommendation | AVERAGE | |
|------------------------------------|-----------------------|-----------------------|
| | 3-Yr TSR (12/31/2014) | 3-Yr TSR (12/31/2013) |
| For | -2% | 8% |
| Against | -16% | -1% |

So far, ISS say on pay recommendations are surprisingly similar to last year, and ISS does not often get credit for being consistent. Factors contributing to the consistent rate of “for” vote recommendations among oil and gas companies seem to be ISS’s new approach to peer group selection for E&P companies, that TSR performance has

generally been poor across the board in certain industry segments (the “low tide” effect), and that companies have begun to adopt pay practices that ISS prefers, such as greater amounts of performance-based LTI or negative TSR governors in relative TSR plans. More specifics on these factors will come to light as we examine pay practices over the coming months as part of annual peer group market reviews.

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